

By the Author of This Volume

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**PRACTICAL BANK OPERATION**

By L H LANGSTON Specific working manual of practice, describing in elaborate detail all operations of banking as carried on in the National City Bank of New York. Covers all departments and functions. Complete working forms.

**BANKING PRACTICE**

By L H LANGSTON and N R WHITNEY Textbook for colleges, based on "Practical Bank Operation," by Langston. Explains comprehensively organization, management, and practical work of a bank.

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# PRACTICAL BANK OPERATION

PREPARED BY

L. H. LANGSTON, M. S.

UNDER THE DIRECTION OF

THE EDUCATIONAL COMMITTEE OF  
THE NATIONAL CITY BANK OF NEW YORK



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## PREFACE

During the past few years there has been a growing desire on the part of the general reading public and of students to know of what goes on inside a bank. This is no illegitimate desire. Of all business institutions perhaps banks come the most closely into contact with the public by virtue of their fiduciary relations. Again, banks in the last decade have extended their services into new fields and it is to the interest of the banks, as well as to that of the public, that as many persons as possible should know of the scope and variety of a modern bank's activities. Furthermore, banks throughout the country are making calls upon schools and universities for new blood, while at the same time the schools are giving increasing attention to a systematic study of banking as a division of modern complex economic life. It is hoped, as one of the purposes of this book, to provide the student with a comprehensive and authoritative exposition of modern banking practice.

There is also a commendable disposition among banks to exchange information about themselves. While the National City Bank makes no presumptuous claims in this connection, yet, because of the innumerable requests for information that are sent in by friends and correspondents all over the world, there is justification for the hope that bankers everywhere may find some advantage in knowing of this bank's method of doing its work. It is also hoped that the National City Bank may have the advantage of whatever criticism its friends may care to make.

In preparing the work the endeavor has been to keep in



mind the needs of three classes of readers, viz · the banker, the special student, and the general reader. The aim is to give an insight, in considerable detail, into the actual work of a large international bank. Each banking operation is set forth herein as it is performed in the National City Bank of New York. No attempt is made to put forward or develop new theories of banking, nor, as a matter of fact, to deal with theories at all. There are in existence already many books which treat this subject in an admirable way. The actual, rather than the ideal, is the subject matter of the present volume.

It is obvious that this plan has its disadvantages. It is virtually impossible to keep such a work up to date. Any organization of considerable size is dynamic rather than static; it is constantly undergoing changes and improvements. Again, one is under obligation to show the defective as well as the good if he would depict accurately the organization of a living institution. No organization is perfect, much less one which, like the bank of today, is just emerging from conditions imposed upon it by international warfare. Nevertheless it is hoped that the advantage of setting forth facts as they are rather than as they will be at some future time, or as an idealist might hope that they could be, will outweigh the obvious disadvantages of presenting the practical side of banking in detail.

The foundations of this book have been long in the making. The original idea found expression a number of years ago in various books for internal use in the bank. To teach the work of the bank to new employees, and old ones as well, was felt to be a most important duty. Accordingly in 1912 Mr J. H. Carter then chief clerk, now vice-president of the bank, with the assistance of department and division heads, prepared a book describing the work of each department. This book was followed in 1914 by a much larger

work which took the form of mimeographed copies of lectures given by department heads and officers before a class in banking made up also of officers and department heads. This work proved so successful that the idea underlying the present book was brought to the front. Why not produce a book which in addition to being useful in the bank's internal educational work would also fit into any educational program which would include those outside the bank as well?

In developing this larger project it was seen that unity would be attained only by employing an editor to devote his whole time to collecting the available material and to preparing the book. Accordingly a man was obtained who was left largely to his own devices in preparing the projected book. The result, while an excellent product, stressed banking history and theory rather than exposition of actual bank operations. A revision of the entire plan of procedure was therefore determined upon.

At this stage in the work the present editor was called, and an editorial committee consisting of Mr. E. E. Agger, then assistant to the president of the bank, Mr. Jacob Wohnsiedler, vice-president, Mr. G. A. Kurz, assistant vice-president, Mr. E. R. Naar, assistant cashier, Mr. E. M. Earle, and Mr. A. L. Billingsley, was chosen to plan and to direct the work.

After a survey of the ground and upon the basis of experience gained from previous efforts, the committee decided that, inasmuch as the material collected by their predecessors had become out of date, it was necessary to build from the beginning. The editor, therefore, with the assistance of Mr. Arno Hoppert and Mr. Harold H. Wylie of the bank's college training class, has studied the work of each department of the bank at first hand and set down herein what he observed. Each chapter of the work has then been submitted to the division and department heads concerned as well as to the

members of the committee and certain other specialists in the bank for criticism and suggestions. A committee consisting of Mr. William A. Simonson, executive manager, Mr. J. H. Carter, and Mr. G. E. Gregory, vice-presidents of the bank has passed upon the book from the standpoint of the management. Mr. Gregory has also made many helpful suggestions of a general editorial nature. The thanks of the committee are also due the New York Clearing House Association for assistance in gathering material for Chapter IV.

From the foregoing brief outline, it is apparent that no one man or small group of men can claim credit for whatever of value there may be in the work. It is a result of joint effort. Practically every officer and departmental executive in the National City Bank has assisted in its production. To them should go the credit, and to them are extended the sincere thanks of the editor and of the committee. If this book has any points of merit, it is a tribute to the co-operative spirit which permeates the organization of the National City Bank. It was this co-operative spirit which alone made the production of the book possible.

THE EDITORIAL COMMITTEE,  
THE NATIONAL CITY BANK  
OF NEW YORK

New York City,  
February 1, 1921.

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PRACTICAL  
BANK OPERATION  

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BOOK I





## CHAPTER I

### THE FUNCTIONS OF A BANK

#### Indispensable Banking Services

The organization known as a bank flourishes in the economic structure because of certain indispensable services it performs. Its work as a whole can best be visualized by an inquiry into the nature of these services, which may be classified as the deposit, the note-issuing, the exchange, the loaning, and the fiduciary or trust functions. These constitute the characteristic functions of a bank. In addition there are such operations as accounting, purchasing, personnel, etc., which may be termed the auxiliary operations.

#### The Deposit Function

The deposit function is first in importance because it prepares the basis for other operations. In performing this function the bank receives cash or its commonly accepted equivalents from its customers, and in exchange it gives them bank credit, that is, the right to draw checks against the amount deposited.

The economic service of the deposit function consists in providing the business community with a convenient medium of exchange which is more desirable than even the money which may give rise to it. As a medium of exchange, money has some disadvantages, among which are the risk of its storage and transportation, the costliness of the basic material from which metallic money is made, the losses from wear and tear in circulation, the difficulty of tracing money as it passes from hand to hand, and many others.

Economic progress has been constantly toward a more and

more satisfactory medium of exchange First barter with all its disadvantages was used, then metallic money, then paper money Finally came the bank check representing the highest development Under a system of exchange carried on by check, the holder of cash or its equivalent exchanges it for bank credit—a thing without substance which, granting that the bank remains solvent, cannot be lost and which cannot waste away in use To use bank credit as a circulating medium, the holder merely draws checks against his balance These may be drawn in the desired denominations, they are drawn upon a material of negligible cost, and they may be readily transported If lost they can be traced and it is next to impossible for anyone but the rightful owner to recover on them Furthermore, a check returns to the drawer who may use it as a receipt for his payment In countries where the system of banking is highly developed the greater part of the actual money in the community is to be found in the banks where it serves as the basis for deposit credit The circulating medium consists principally of checks drawn against these deposit credits

A bank can successfully induce its customers to exchange their cash or its equivalent for bank credit so long as this credit is more attractive to them than the actual cash with which they are to part As noted in the preceding paragraph, a variety of factors enter into the attractiveness of bank credit—its divisibility into convenient units, its portability, its wide acceptability, its security, etc Most important of these is security

The security of bank credit is the safety of the bank itself and a discussion of the elements which contribute to such safety would lead the present discussion far afield So far as the depositor is concerned, the safety of bank credit depends upon the bank continually keeping on hand the wherewithal to meet the checks which he may draw and its actually

meeting all proper demands made upon it. In other words, depositors entrust their funds to the bank because they feel certain that they can obtain the return of an equivalent amount when they desire. Hence the bank's paying operations, which consist in keeping on hand a supply of lawful money and in paying checks when they are presented, may be considered as a component part of the deposit function.

### **Note-Issuing Function**

If the bank under consideration is a bank of issue, it may make a part of its payments in its own bank notes. Then the note-issuing function comes into operation. In the United States a national bank may exercise this function by purchasing and lodging as security with the United States Treasury, government bonds of certain issues. It is then permitted to issue its notes in an amount equal to the par or market value of the bonds, whichever is lower, provided the amount of such issue does not exceed the paid-in capital of the bank. While the privilege of note issue is used more or less extensively by the national banks of the country, this function is gradually being taken over by the federal reserve banks.

### **The Exchange Function**

The exchange service performed by a bank may be explained by illustration. Let it be supposed that a merchant in St. Louis, Missouri, has purchased a bill of clothing amounting to \$6,000 from a New York manufacturer. When the bill falls due the buyer settles by sending the New York manufacturer his check drawn upon a St. Louis bank. This check is St. Louis funds, i. e., it is payable in St. Louis, and without the exchange service of banks the holder in New York would be put to the inconvenience of either sending the check to St. Louis and having the bank there ship him actual money, or of searching New York until he found someone who owed

a debt in St. Louis and was willing to purchase the check for the purpose of making remittance. Under a system of highly developed exchange carried on by the banks, the holder of the check is put to no such inconvenience. He merely deposits it in his New York bank. He receives New York funds in exchange for it, i.e., the right to draw checks against the New York bank to a corresponding amount, less, perhaps, a small fee, and he is not concerned further with the transaction except for his contingent liability as an indorser on the check.

The exchange transaction may take a variety of forms. If the payment must be made in haste the buyer might have his local bank telegraph its New York correspondent to pay the creditor the desired amount. Again he might purchase a draft drawn on a New York bank and remit it to his creditor. Instead of the St. Louis merchant taking the initiative and sending a check, the New York merchant may draw a draft on him for the amount of the indebtedness. The drawer of the draft would then leave it with his local bank for collection. Transplant the St. Louis merchant to Rio de Janeiro, Brazil, and foreign exchange arises. Yet the principle is the same in all cases. The bank makes local funds available in exchange for distant ones, or vice versa.

The exchange transaction may involve the mere bridging of distance, as in domestic exchange. In performing the foreign exchange function, however, the exchange transaction has a wider significance. It involves not only bridging distance, but also differences in monetary standards and national customs.

In the aggregate the exchange operations of banks perform the highly useful service of clearing international and inter-sectional claims and credits. Let the exchange transaction between the St. Louis and the New York bank mentioned above be considered again. It has been noted that the New

York bank exchanges New York funds for St. Louis funds. These St. Louis funds it converts into New York funds by charging the account of a St. Louis bank or by receiving a remittance in New York funds from St. Louis. Were such transactions to continue in this one-sided way, the supply of funds standing to the credit of the St. Louis bank would soon be exhausted and it would be necessary for it to ship money to New York. The transaction is not one-sided, however. Customers of the St. Louis bank are constantly presenting claims payable in New York to their local banks in exchange for local funds. These are sent to New York where they are applied to building up the balance to the credit of the St. Louis bank, i.e., its supply of New York funds.

If now the illustration be extended to include the exchange dealings of the banks of a whole community or country with those of another, it is apparent that the claims of the one are made to offset those of the other. Only balances need be settled by shipments of money. If, as is usually the case, the claims tend in the long run to be equal, it will be unnecessary to ship money at all.

### **The Loan Function**

When a bank exchanges present funds for future funds the transaction is a loan or a discount. Consider again the situation of the New York manufacturer. In the fall he may need to make outlays for materials and labor in order to manufacture for the spring demand. If he is a progressive business man he may desire to expand his business beyond the limitations of his own funds. He raises the needed funds by borrowing at his bank. On the strength of its estimate of his honesty and his ability as a business man the bank loans him the required amount, taking in exchange his note drawn to mature when the manufactured product is sold and the proceeds of the sale are available.

Strictly speaking, the bank's economic service here is that of exchanging present funds for future funds—that of bridging time. Under the capitalistic system of production there is an interval of time between the outlay and the income. The manufacturer makes outlays for materials and labor, later he receives the proceeds from the sale of finished goods. The merchant makes his outlay for merchandise at wholesale, and after paying wages and expenses of exhibiting and selling the goods, he is reimbursed by their sale. In the spring the planter makes his outlay for cotton seed, and during the summer for labor, expecting the whole outlay to be returned in the fall in the form of the ripened crop. It is in bridging this characteristic gap between the outlay and the income of funds used for production that the bank performs one of its chief economic functions.

In exercising this loaning function a bank goes beyond the mere bridging of time. It places the funds of those who are not disposed to use them at the disposal of those who are. Persons who have funds which they are not using temporarily, deposit them with some bank, possibly on a time arrangement. The bank uses these idle funds as a basis for supporting loans to those who need funds to carry on their operations. Thus, in the first place, the full usable capital of the community is kept constantly employed. In the second place, the handicap of a relative lack of capital is removed from those who otherwise are equipped to succeed in a business way.

Herein lies perhaps a bank's greatest service, and at the same time its heaviest responsibility. Under a system of free banking it may be said that no man need be seriously restricted in his economic endeavor by lack of capital alone. If he is worthy of trust, if his enterprise is legitimate and well chosen, there is always a bank willing to advance him the funds he needs. The fact, however, that a bank uses the

funds of others to whom it must account for every dollar, demands that each enterprise which it stands behind in a financial way be chosen with unerring judgment as to its successful outcome. This very fact operates toward the economical employment of the funds of the community in successful enterprise. It is a check against misguided projects with their resultant waste of capital.

Finally, in exercising their loaning function banks add to the volume of funds available for use in the community. They act as manufacturers of usable funds. To illustrate this service of a bank, a hypothetical case may be considered. Suppose that a bank begins business with a capital of \$1,000,000 and a surplus of \$100,000 fully paid in cash by the stockholders. Its financial position would be

Cash	Capital and Surplus
\$1,100,000	\$1,100,000

Owing to the business reputation of the incorporators and to the convenience of having funds in the form of bank credit, it can be assumed that this bank will attract net cash deposits of perhaps \$4,000,000. That is, customers of the bank would leave on deposit with it on the average of \$4,000,000. Under these circumstances the bank's financial position would show

Resources		Liabilities	
Cash	\$5,100,000	Capital and Surplus	\$1,100,000
		Deposits	4,000,000

Thus far the function of the cash, \$5,100,000, shown on the asset side of the statement is solely to act as a reserve fund to meet checks drawn against the \$4,000,000 deposits on the liability side. It is apparent that this amount is far in excess of requirements. At no one time will all the depositors withdraw their balances in full. The bank needs to keep on hand only an amount of cash slightly in excess of what



they do withdraw. Each bank arrives at this figure by experience and expresses it in the form of a ratio termed the "reserve ratio." Let it be supposed that the hypothetical bank decides upon a high ratio of 20 per cent. Then it would need to keep on hand a reserve of 20 per cent of \$4,000,000 (the amount of deposit liability outstanding), or \$800,000. From its balance sheet shown above, the idle cash would be the difference between \$5,100,000, the cash actually held, and \$800,000, the cash needed as reserve, or \$4,300,000.

The bank now begins to engage in the loaning business. Suppose every borrower asked for and received cash at the time his loan was made. The capacity of the bank to carry loans would be \$4,300,000 and its balance sheet would be as follows:

Resources		Liabilities	
Cash	\$ 800,000	Capital and Surplus	\$1,100,000
Loans and Discounts	4,300,000	Deposits	. . . 4,000,000

As a matter of fact borrowers do not desire actual cash. They take credit on the books of the bank, which has the same attraction for them as for those who actually deposited cash in exchange for bank credit. Loans build up deposit liability. Let it be supposed that those who are borrowers at the bank receive credit on its books for the full amount of their borrowings, and of the amount so credited (\$4,300,000) they maintain average balances of \$2,000,000. The position shown in the preceding paragraph, would now be changed to:

Resources		Liabilities	
Cash	\$2,800,000	Capital and Surplus	\$1,100,000
Loans and Discounts	4,300,000	Deposits	. . . 6,000,000

The bank now has a deposit liability of \$6,000,000 against which it holds \$2,800,000 cash, not to mention loans and discounts which will mature shortly. Its experience shows

that it needs only 20 per cent of \$6,000,000, or \$1,200,000 cash, instead of the \$2,800,000 which it holds. There is, therefore, an excess of \$1,600,000. On the basis of \$1 reserve cash to each \$5 of deposits liability, this excess is sufficient to support additional loans to the amount of \$8,000,000 more and the bank's financial position becomes

Resources		Liabilities	
Cash	. \$ 2,800,000	Capital and Surplus	\$ 1,100,000
Loans and Discounts	12,300,000	Deposits	. 14,000,000

This illustration is not given with the object of showing the true loaning capacity of a bank. It omits many factors which must be taken into consideration. The idea is rather to show that a bank makes more funds available for the community than it actually has entrusted to it. In the illustration the bank has the use of only \$5,100,000 actual cash. This is safely expanded into loans and discounts amounting to \$12,300,000. In other words, the business community, including its own shareholders, entrusts the bank with \$5,100,000 and this same community receives in return the use of \$12,300,000.

### Fiduciary or Trust Functions

On account of their experience and fitness for handling financial affairs, many banks act in a fiduciary capacity for their clients. In exercising this function the bank becomes the holder of property which it is to use according to the instructions of the trust. Property is kept productive without wastage and the principal as well as the increment is applied impartially according to the desires of the person who entrusted it to the bank. The economic service rendered is that of perpetuating the will or desires of those who have property. The corporate mind of the bank with its fairness, its permanency, its skill, and its firmness, is substituted for the perishable human mind.

### Auxiliary Operations

The functions so far described may be termed the characteristic banking operations. In any business organization, however, there are in addition to its characteristic functions certain operations which must be performed to facilitate the characteristic ones. These auxiliary functions are accounting, purchasing, employment, research, correspondence, organization, administration, etc. While they vary in different types of business, their essentials are the same with all. These operations are also found in a bank.

### Summary of Banking Functions

In summary it may be said that a bank is chiefly a manufacturer of credit. Its raw material is the credit instrument held or produced by its clients. In their raw state these instruments have certain undesirable features which induce their holders to part with them. They may be payable in the future when present funds are wanted. They may be payable in a foreign monetary unit when domestic funds are wanted. They may be payable at some distant point when local funds are desired. A holder may have money when deposit credit would serve his purpose better. In exchange for all these forms of raw material the bank gives its own credit, in whatever form is most useful to the particular client.

In this book the purpose is to show how a particular institution, the National City Bank of New York, performs the functions just enumerated.

## CHAPTER II

### THE RECEIVING OPERATIONS

#### General Statement of Receiving Operations

The process of receiving deposits is probably more nearly an initial banking operation than is any other. It is a process of operating upon raw material in the sense that the items received come from outside the bank. Again the receiving operation is an initial one in the sense that it sets many others into motion. Such operations as clearing checks, keeping and caring for cash, collecting city and transit items, etc., are the direct consequents of the operation of receiving items on deposit.

In a somewhat less direct way the principal function of the bank, viz., that of making loans, is dependent upon the receiving operations for support. It would not be true to say that the bank builds up a fund of cash through its receiving operations and then passes this fund out to borrowers, for borrowers do not, as a rule, ask for or receive the proceeds of their borrowings in cash. They receive instead credit on the books of the bank. In other words, loans create deposit liability. The amount of deposit liability which the bank can incur in exchange for customers' notes in this way is, however, limited by reserve requirements. Normally, cash reserve for supporting deposit liability is accumulated and maintained largely through the receiving operations. The relationship between the receiving operations and the loaning operations is, accordingly, thus: the receiving operations build up and maintain a cash fund, this cash fund becomes cash reserve, the possession of cash reserve gives the bank capacity for

building and expanding its deposit liability, deposit liability is in turn expanded through the loaning operations. Thus the results of the receiving operations support and limit the loaning operations.

### **Nature of Receiving Operations**

At the outset a distinction must be made between cash items and collection items. When a customer of the bank makes a deposit he exchanges certain items for immediate credit on the books of the bank. These become the property of the bank and are spoken of as cash items. On the other hand, when a customer leaves items for collection he merely employs the bank as his agent. Immediate credit to his account or payment for the collection is not given, the bank agrees to make the proceeds available for the customer's use only after collection has been effected. An item of this sort is termed a collection item. A distinction between these two classes of transactions is important because of the fact that the bank sets up different machinery for handling each. The receiving operations, which are the subject of this chapter, involve exclusively the handling of cash items.

In planning its organization to care for the work of receiving deposits a bank has in mind chiefly service requirements. Local customers bring their deposits in person or send them by messenger. They must be accommodated by courteous and attentive window service. Out-of-town depositors, however, must have an entirely different type of service, since their deposits come by mail or express. Depositors in the bank's foreign department likewise require a distinct type of service. To care for these demands the bank is organized for receiving deposits as follows: first, there is a receiving teller's department which attends to receiving the deposits of local customers, second, there is a mail teller's department which cares for receipts from out-of-town depositors, and

third, there is a receiving section in the foreign teller's department which receives items for the credit of foreign accounts

### **Function and Organization of Receiving Teller's Department**

The work of the receiving or second teller's department is more or less known to the average reader, for a receiving teller's department is to be found in all banks save the very smallest. The function of this department is to receive and receipt for, prove, record, and distribute the cash items which customers deposit over the window.

The work of the receiving teller's department consists of two parts: receiving deposits at the window, and proving, sorting, and distributing the receipts. Since the function of this department is to serve the local customers of the bank, the organization is determined by the needs of these customers. Customers of a large down-town bank make relatively few deposits in number, although the individual deposits are as a rule large in size. The window work of the department is performed, therefore, by a small force of tellers.

The second phase of the work, which consists in proving and distributing the cash items received, is performed for the most part in the afternoon. During the morning the work of the department is comparatively light as depositors generally follow the custom of making their deposits near the close of the business day. In the morning, too, those departments of the bank which depend upon the receiving teller and the mail teller (who receives the deposits which come by mail) to furnish them with the raw material for their day's work are occupied with the heavy early morning receipts of the mail teller. Under these circumstances only the relatively few extra large items are passed completely through the sorting, proving, and distributing process of the receiving teller's department early in the day. Most of the material is held over for the afternoon. In the afternoon certain clerks are

released from those departments which have the heavy part of their work to perform in the morning, and these clerks, acting under the direction of a member of the receiving teller's department, attend to the work of sorting, proving, and distributing the day's receipts.

### **Incoming Deposit**

Before making his deposit the customer indorses his negotiable instruments (checks, drafts, etc.), counts his money, and prepares a deposit slip. Depositors are in most cases familiar with the requirements of the bank as to what specific items it will receive on a cash basis and what items it will take on a collection basis only. Upon the deposit slip the former only are listed. They include currency, checks, sight drafts, certified checks, and coupons from United States bonds. Occasionally other items may be received on a cash basis by special arrangement.

### **Examination of Deposit**

It is apparent that somewhere in the banking process the deposit slip and each item contained in the deposit must be carefully examined—the deposit slip for accuracy, and the items for such defects as faulty or missing indorsement, stop-payment orders, insufficient funds, forgeries, alterations, etc., in the case of checks, and inaccuracy of count, alterations, and counterfeits in the case of money. It is equally apparent that it is impossible and impracticable for the window man to attend to all these matters of scrutiny. This situation is met by shifting the burden of making examinations to others in the department and to other departments which receive the material after it has passed through the hands of the receiving teller. For example, the proving force of the department verifies the accuracy of the deposit slips. Likewise the bookkeepers have the duty of detecting all check-

drawn on the bank which it cannot pay because of stop-payment orders, insufficient funds, forgeries, alterations, and missing indorsements, while the money department has the responsibility of examining and passing upon all money received into the bank. Under a system of this sort the receiving teller serving at the window examines the deposits only for those defects which cannot be readily discovered afterwards; the deposit is received subject to correction, should the need arise

### Exchange Charges

As a general thing, in handling exchange charges the practice in the bank is to have the transit department assess the exchange charges when it sends the country items out for collection (See page 119.) Some depositors, however, prefer to pay exchange at the time of making their deposits, and in a case of this kind the receiving teller accepts the payment. He credits the note teller for such exchange collected since the note teller keeps the account for exchange paid over the window. Upon receipt of notice of this credit from the receiving teller, the note teller credits the bank's exchange account and debits the receiving teller for the amount of the exchange. The receiving teller also prepares a list of his receipts for the transit department to prevent the latter department from charging the exchange a second time in the regular course of its business.

### Depositor's Receipt

After the deposit has been accepted the customer is given a receipt for the amount. This receipt takes the form of a pass book entry, or a duplicate deposit slip. The receipt is an evidence of a credit to the depositor's account subject, of course, to corrections. The depositor leaves the bank with the right to draw checks against the deposit, while the bank



has increased its holdings of cash or cash items to a corresponding amount

### **Despatch of Special Items for Collection**

As has already been noted, the majority of the deposits are retained in the department until the afternoon when a separate force proves them, and sorts and distributes the constituent items throughout the bank. Frequently, however, items are received which it is advisable to rush through the collection process without waiting to make a proof. For example, the bank saves interest for one day if it rushes items through the clearing house, the transit department, or the city collection department upon the day of receipt rather than upon the following day, as would be the case if the items remained in the receiving teller's department until the afternoon. Such items, accordingly, are sent immediately to the departments which are to collect them. Likewise large pieces of currency are immediately turned over to the paying teller, who has the custody of the cash of the bank. To replace any items which may have been withdrawn from the deposit for reasons of this nature, a "take out and charge" ticket is prepared in order that the proof may be complete.

### **Sorting, Proving, and Distributing the Receipts**

The object of the sorting, proving, and distributing processes is, first, to distribute the items received to other departments of the bank for attention without delay, second, to obtain journal entries for the transactions passing through the department in order that they may be recorded in the general ledger, and third, to prove the accuracy of both the journal entries and the customers' deposit slips.

The constituent elements in a particular deposit consist of (1) the deposit slip, and (2) the cash items making up

the deposit. The deposit slip is used to represent the credit to the depositor's account, while the items themselves are a debit to cash

### Disposition of Credit Items

To facilitate the work of the ledger bookkeepers the deposit slips are divided into groups according to the subdivisions of the depositors ledgers, and those contained in each group are sent to the bookkeeper in charge of that ledger as soon as a convenient amount has accumulated. The receiving teller's department retains a triplicate record of these sendings. One copy of this record is forwarded to the statement clerks of the bank to serve the purpose of original data for posting to the customer's statement of account (see page 542), a second copy accompanies the deposits which it represents through the proving process, and the third copy becomes the basis of a report to the general bookkeepers of the bank, showing the total credits sent by the receiving teller to each depositors ledger. (See Form 1.)

### Proof of Receipts

The work of proving the deposits is performed by a separate force. The basis of the proof is the batch, which consists of a volume of duplicate deposit slips and their offsetting cash items of convenient size for working.

The various items making up the batch are sorted into two divisions—the credits, or interdepartmental deposit tickets, in the one division, and the debits or cash items, in the other. The debits are then divided into the following categories:

- 1 Clearing house items—checks and other instruments drawn payable by banks which clear through the New York Clearing House
- 2 Checks drawn upon the bank itself (these are called "Eights" in the work of the National City Bank

of New York, since the clearing house number of this bank is eight)

- 3 Sights—drafts drawn upon city diawees not reached by the city collection department of the New York Clearing House

DATE			
RECEIVING TELLER	<u>December 31 1921</u>	CREDITS	
Domestic Individual Ledgers			
Alabama—Idaho	1,316,208.06		
Illinois—Louisiana	718,200.00		
Maine—Missouri	301,042.10		
Montana—Ohio	1,101,311.14		
Oklahoma—Penn a	2,016,341.17		
Rhode Island—Wyoming	2,410,001.04		
New York City A	6,427,382.60		
" " " B	4,147,834.01		
" " " C	7,304,261.18		
" " " D—F	5,010,731.42		
" " " G—I	1,178,100.00		
" " " J—L	4,332,401.03		
" " " M—N	2,106,218.60		
" " " O—R	547,188.25		
" " " S	1,003,166.05		
" " " T—Z	3,141,121.13		
	TOTAL	4,306,150.78	
Missouri—New York		5,050,479.68	
	TOTAL	48,112,487.46	

- 4 Trusts—drafts drawn upon city drawees which can be reached through the city collection department of the clearing house
- 5 Small countries—checks under \$500 drawn on out-of-town banks These appear only in the afternoon work when “small countries” are sorted separately from “large countries” listed below, because the small items are to be laid aside for the night force of the transit department in order that the undivided attention of the afternoon force may be given to sending the large countries for collection.
- 6 Large countries—country checks contained in the afternoon work which are large enough to make it profitable to pay special attention to despatching them for collection on the day of receipt
7. Cash—the money itself will have been taken out of the deposit and this item will consist of cash tickets substituted therefor
- 8 Checks drawn upon banks for which this bank clears
- 9 Large sight drafts—city items of a size large enough to make it profitable for the bank to collect them by messenger on the day of receipt

The proof clerks make a separate list of the items contained in each of these categories, attaching each list to its proper group They then prepare a proof of the batch (Form 2) The principle of the batch proof is to be found in the axiom that the whole is equal to the sum of its parts. One part of the proof shows the distribution of the debit items according to the categories shown above, the other gives the total credits making up the batch subdivided according to ledgers The sum of the deposit tickets must equal the sum of the contents of the deposits When the batch proof is thus found to balance, the items contained in the batch

Sorted by <i>Robert Eddy</i>			
Listed by <i>John Kelly</i>			
<i>Clearing House</i>	Division A 1-23	140	431 14
	Division B 28-45	35	140 67
	Division C 59-76	38	283 49
	Division D 77-100	21	769 56
	Division E 102-120	371	521 16
	No 8	39	692 01
	Sights		77 01
	Trust Co's	8	568 44
	Small Countries	5	183 50
	Large "	76	260 88
Cash	1	365 05	
8 Sights	6	098 59	
F X 8		872 30	
Large Sight Drafts	219	000 00	
Total		964	264 30
<i>New York A 6</i>		<i>457</i>	<i>048 66</i>
<i>New York B 6</i>		<i>293</i>	<i>405 00</i>
<i>New York C 4</i>		<i>29</i>	<i>406 07</i>
<i>New York D F 8</i>		<i>184</i>	<i>404 57</i>
<i>Total</i>		<i>964</i>	<i>264 30</i>

Form 2. Receiving Teller's Batch Proof (Size  $5\frac{1}{2} \times 8\frac{1}{2}$ .)

"8 sights" means drafts drawn on banks for which the bank clears, "F x 8" those drawn on the foreign division of the bank

are ready to be passed on to the other departments of the bank. If in proving the batch it is discovered that the customer has made an error in his deposit slip, a correction ticket is sent to the ledger bookkeeper and the customer is advised of the error.

### **Disposal of Debit Items**

After the various debit items have been proved they are disposed of to the different departments of the bank as follows.

1. The clearing house checks are charged to the paying teller but sent to the assembly rack
2. The checks drawn upon the bank itself are charged and sent to the check desk
3. The sights, trusts, small countries, and checks upon banks for which the bank clears are charged to the city collection department, but the small sights, trusts, and small countries are sent to the transit department to be sorted by the night force
4. The large countries are charged and sent to the transit department
5. The cash is charged and sent to the paying teller

### **Receiving Teller's Daily Proof**

A departmental daily proof may be defined as a record of the changes in the accounts of the bank occasioned by the work which passes through a department on a given day. In addition to requiring regular entries on the books of the bank to cover charges in assets and liabilities, income, expenditures, etc., bank accounting calls for a detailed record of the cash items as they pass from one banking process to another. Accordingly each operating department prepares a proof in which it gives credit to every other department of the bank for the aggregate amount received from that department, and to the accounts of the bank as well for credits made

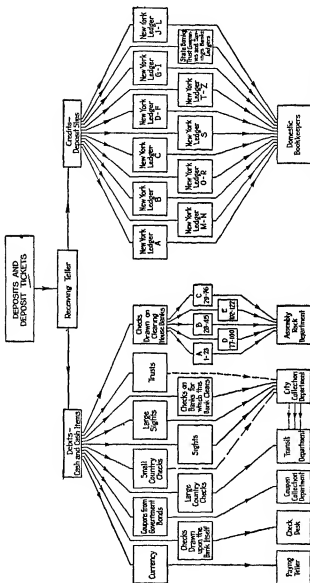
to them. Likewise the department debits other departments for cash items which have been passed to them during the day and the accounts of the bank for charges which have been made to them. A departmental proof is therefore a

SECOND TELLER'S PROOF, Dec 31 1921.					
Transit Dept.	2, 975, 530	51	Deposits,	48, 112, 488	46
Check Clerk No. 8,	12, 186, 400	23			
Paid to 1st Teller	36, 763	97	Rec'd from 1st Teller,		
" 3rd "			" 3rd "		63
" 4th "	942, 170	44	" 4th "		
" 5th "			" 5th "		
Large Sight Drafts,	539, 638	86			
Small Countries	890, 047	09			
Sight Drafts	660, 721	23			
Trust Co's,	1, 423, 366	14			
Clearing House Exchanges,	28, 457, 829	62			
Total,	48, 112, 488	09	Total,	48, 112, 488	09

Form 3 Receiving Teller's Daily Proof (Size  $8\frac{1}{4} \times 8\frac{1}{4}$ .)

condensed journal record of the entire work of a department for a given day.

In keeping with such an arrangement the receiving teller assembles his batch proof figures into a trial proof from which the departmental proof (Form 3) of the day's operations is prepared. On Form 4 is shown the disposition of



Form 4 Chart Showing Disposition of Items Passing Through Receiving Teller's Department

Sights trusts and small country checks are held overnight. Hence they appear on the city collection department proof since this department maintains the hold-over account. The checks themselves, however, are sent direct to the transit department where they are prepared for collection the following day.



the various items that pass through the receiving teller's department during the course of a day's work

### **Mail Teller's Department**

The mail teller acts as a receiving teller for deposits from out-of-town domestic customers. Accordingly it is the chief function of the mail, or fourth teller's, department to receive, prove, record, distribute, charge, and acknowledge the cash items which come to the bank by mail. Incidentally all ordinary mail which is addressed to the bank passes through this department for examination. Those letters which contain cash remittances are retained and they become the material upon which the department works. Non-cash letters are passed on to others for distribution throughout the bank. Letters containing items which are to pass through the work on a collection basis are handled by the mail teller, but simply in a preliminary way, and they are only incidental to the regular work of the department. Another incidental function is that of preparing the morning exchanges for the clearing house. This work will be described in the chapter on the clearing operations (Chapter IV).

A mail teller's department is not found in small banks nor in many large ones, for the volume of the work is not so large that the receiving teller cannot handle it economically. A bank having extensive out-of-town connections, on the other hand, has a volume of incoming mail large enough to make such a department a necessity. Part of the mail consists of ordinary deposits received from out-of-town individuals, firms, and corporations who are customers of the bank. The larger part, however, comes from correspondent banks and represents items which these banks are collecting by depositing them with their city correspondent. The mail teller's department is therefore an organization to be found mainly in large bankers' banks.

### Divisions of Day's Work

The day's work in the mail teller's department is divided into three major divisions. viz , the night mail, the morning mail, and the afternoon mail, each of which is handled as an individual unit. The night mail consists of letters received from the post-office subsequent to the closing hour of the day before, and of "hold-overs," or items retained from the previous day's work. By beginning on the day's work before the bank opens, the mail teller's department not only makes it possible to complete its own work during the day of receipt, but it also evens up the flow of work into the other departments.

An important function of the morning section is to prepare as many items as possible for the clearing house session at ten o'clock. Accordingly this section includes all letters which have come from the post-office since the night mail force completed its work, together with those items which other departments of the bank, such as the receiving teller, the paying teller, etc , have received before ten o'clock, and which they are able to send to the mail teller in time for the clearing house session on the same day. The morning section also handles morning items for those banks which use the bank under consideration as their clearing agent. The afternoon mail consists of all letters received after the morning mail has been completed.

The night mail is handled in precisely the same manner as is the morning mail. The handling of the afternoon mail differs from that of the morning mail chiefly in the disposition of the items through the bank, and this part of the work follows closely the routine of the receiving teller's department. Nothing would be gained by describing each division separately. The following discussion of the routine of the mail teller's department will, then, describe the work of a single division—the morning mail.

### **The Morning Mail**

Handling the morning mail is the main event in the day's work of the mail teller's department. Literally thousands of letters, containing thousands more of enclosed items, come into the department for attention at this time. Moreover, only two hours are available for completing the whole mass of work, if the bank wishes to send the clearing house items contained in the letters through the clearing house on the day of receipt. It is also necessary that the other operating departments of the bank receive their work from the morning mail in time to complete it before the items of the receiving teller begin to come in in large numbers. To meet this situation the mail department expands to several times its normal size by drawing additional workers from various departments in which the early morning work is light.

### **Opening the Mail**

The mail comes first to a force of openers who carefully examine each letter for cash enclosures. This force lays aside for other departments those letters which do not contain cash items, as they bear no further relation to the work of the mail teller. Each examiner places a numbered stamp, which has been assigned to him for the day, upon the back of each letter. Responsibility for error in examining the letters is thus fixed upon the one who made the examination. After opening the letters the clerks clamp each cash letter with its enclosures and pass it to the sorting force.

### **Sorting the Mail**

The sorters divide the letters into sections according to the division of labor under which the department operates, as follows

Section 1 Letters to be credited to accounts found in

the national bank ledgers, Alabama—Idaho, Illinois—  
Kansas, Texas—Wyoming

Section 2 Letters to be credited to accounts found in  
the national bank ledgers, Kentucky—Mississippi,  
Missouri—New York

Section 3. Letters to be credited to accounts found in  
the national bank ledgers, North Carolina—Oklahoma,  
Oregon—Tennessee

Section 4 Letters to be credited to accounts found in  
the state bank, trust company, and savings bank ledgers,  
Alabama—Illinois, Indiana—Mississippi

Section 5 Letters to be credited to accounts found in  
the state bank, trust company, and savings bank ledgers,  
Missouri—New York, North Carolina—South Dakota,  
Tennessee—Wyoming, letters to be credited to the  
accounts contained in the individual ledgers, and credits  
for the collection ledgers

### Work of the Rack Forces

To handle the work contained in each section mentioned above, a rack force is in operation. The term "rack" denotes a box of pigeonholes into which items are sorted, but the term has also come to connote that part of the work which is performed by the force which sorts items into the rack. Thus the terms "afternoon rack," and "assembly rack," etc., are used. Each rack force of the mail teller's department operates as a unit. The work is exactly the same for each one and consists of proving the letters, sorting the enclosures for distribution throughout the bank, and preparing a proof of the work of the section as it is completed. A description of the work of one section will therefore suffice for all.

As soon as a convenient volume of work for any one section has accumulated in the hands of the sorters it is segregated and a "batch" or "block" is taken to the force

### **The Morning Mail**

Handling the morning mail is the main event in the day's work of the mail teller's department. Literally thousands of letters, containing thousands more of enclosed items, come into the department for attention at this time. Moreover, only two hours are available for completing the whole mass of work, if the bank wishes to send the clearing house items contained in the letters through the clearing house on the day of receipt. It is also necessary that the other operating departments of the bank receive their work from the morning mail in time to complete it before the items of the receiving teller begin to come in in large numbers. To meet this situation the mail department expands to several times its normal size by drawing additional workers from various departments in which the early morning work is light.

### **Opening the Mail**

The mail comes first to a force of openers who carefully examine each letter for cash enclosures. This force lays aside for other departments those letters which do not contain cash items, as they bear no further relation to the work of the mail teller. Each examiner places a numbered stamp, which has been assigned to him for the day, upon the back of each letter. Responsibility for error in examining the letters is thus fixed upon the one who made the examination. After opening the letters the clerks clamp each cash letter with its enclosures and pass it to the sorting force.

### **Sorting the Mail**

The sorters divide the letters into sections according to the division of labor under which the department operates, as follows

Section 1. Letters to be credited to accounts found in

the national bank ledgers, Alabama—Idaho, Illinois—Kansas, Texas—Wyoming

Section 2 Letters to be credited to accounts found in the national bank ledgers, Kentucky—Mississippi, Missouri—New York

Section 3 Letters to be credited to accounts found in the national bank ledgers, North Carolina—Oklahoma, Oregon—Tennessee

Section 4 Letters to be credited to accounts found in the state bank, trust company, and savings bank ledgers, Alabama—Illinois, Indiana—Mississippi

Section 5 Letters to be credited to accounts found in the state bank, trust company, and savings bank ledgers, Missouri—New York, North Carolina—South Dakota, Tennessee—Wyoming, letters to be credited to the accounts contained in the individual ledgers, and credits for the collection ledgers

### Work of the Rack Forces

To handle the work contained in each section mentioned above, a rack force is in operation. The term "rack" denotes a box of pigeonholes into which items are sorted, but the term has also come to connote that part of the work which is performed by the force which sorts items into the rack. Thus the terms "afternoon rack," and "assembly rack," etc., are used. Each rack force of the mail teller's department operates as a unit. The work is exactly the same for each one and consists of proving the letters, sorting the enclosures for distribution throughout the bank, and preparing a proof of the work of the section as it is completed. A description of the work of one section will therefore suffice for all.

As soon as a convenient volume of work for any one section has accumulated in the hands of the sorters it is segregated and a "batch" or "block" is taken to the force

which handles the rack for that section. The first task of each rack force is to determine that the items have been properly sorted to them. Those which belong to some other rack, but have been sorted to a given rack in error, are listed on the "in and out" proof of the department as an "out" to the rack receiving them in error, and as an "in" to the proper rack. The rack forces also examine each letter to see that it is addressed to their bank, i e., that it has not been sent in error.

### Elimination of Collection Items

Mention has already been made of the fact that the mail teller is concerned with collection items only in a preliminary way. The rack forces accordingly eliminate the items which have been sent to the bank on a collection basis rather than on a deposit or a cash basis. The letters may contain only cash items, only collection items, or both. The collection items are deducted from the footing of the cash letter, if they are included therein, and listed on a special interdepartmental letter which shows the name of the customer, the date, the face amount of the item to be collected, and any special instructions received, such as advising payment by mail or by telegraph and instructions as to protest. All collection items are then entered in a blotter and turned over to representatives of the departments which are to collect them, as follows:

- 1 The coupons, to the coupon collection department
- 2 The out-of-town items, to the country collection department
- 3 Notes, to the note teller.
- 4 Time drafts, documentary drafts, collections for those having no account with the bank, trade acceptances, items requiring special advice to the customer, and other items payable in the city, to the city collection department.

When all have been accounted for as having been delivered to the proper departments for attention, the mail teller's department is no longer concerned with collection items. The receipt of all such collection items, however, is acknowledged by the mail teller in connection with the advising of cash item receipts.

### **Proof of Batch**

After the collection items have been eliminated the cash items are proved. The contents of the batch are divided into two parts, the letters, representing the credits to customers' accounts, and the enclosed items, representing the debits to cash. The debit items are then subdivided according to the disposition which the department is to make of them after proving them. These subdivisions, which have the same significance as those used by the receiving teller, are as follows:

- 1 Clearing house
- 2 Checks on the receiving bank itself.
- 3 Trusts
- 4 Sights
- 5 Countries
- 6 Miscellaneous—currency, exchange, cash, and collection return items

Members of the rack force add and list the items in each of these six divisions of the debits and make them up into packages. A batch proof is then made which is similar to that used by the receiving teller's department (Form 2, page 22).

The sixth division contains items which perhaps should be explained more fully. Whatever currency the mail teller receives generally comes to him through error of the remitting bank in sending by ordinary mail currency which it intended to send by registered mail or by express. This is charged and turned over to the paying teller.



### Exchange and Collection Items

Exchange in connection with collection items consists of charges which have been made by country bank correspondents for collecting items sent to them by the bank through the transit and the country collection departments. Out-of-town correspondents settle with the bank for the proceeds of items which they collect for it either by sending a remittance or by retaining the amounts collected and having their accounts charged. In case the item sent for collection is a cash item and the second method of settlement is to be used, the bank charges the whole amount of the sending to the account of the proper collecting correspondent without waiting for advice from the correspondent regarding the charges made. When a bill for exchange charges covering a transaction of this sort is received, the bill is paid by simply sending it to the bookkeeper to be posted to the credit of the correspondent's account.

When items are sent to a correspondent for collection on other than a charge basis, debit for the face amount of the sending is made to a special account maintained with the correspondent in the collection ledger. After collection has been effected the correspondent makes settlement by sending a remittance for the face of the collection less its charges for exchange. In order that the entry in the correspondent's collection account may be closed out, the exchange is added to the remittance letter which is then sent to the collection ledger for posting to the credit side of the account.

The mail teller's exchange charges are listed on exchange sheets and at the close of the day a ticket charging exchange for the full amount is drawn. After this ticket has been audited it is posted as a debit to the Exchange account.

### Cash and Collection Returns

Cash return items are checks, drafts, etc., which previously were sent out by the bank's transit department and charged

to the accounts of correspondents. Because of insufficient funds, stop-payment orders, forged signatures, and other irregularities, the drawee banks have refused to pay them. The correspondents, therefore, charge them back and ask the receiving bank to credit their accounts where it previously debited them. The remittance letter constitutes the basis for crediting the correspondent's account and is sent to the bookkeepers for credit in the regular way. The dishonored item is charged and sent to the city collection department which has the duty of recovering the amount involved from the customer who deposited the item.

Collection returns, like cash returns, are those which out-of-town correspondents have failed to collect. They were not charged to account when they were sent out, however, hence no credit is to be made to the correspondents' accounts except for protest fees which may have been paid. Such fees are credited to the account of the correspondent which sustained them and charged to the city collection department, which department has the duty of recovering from the customer who sent the item for collection. In case no protest fees have been incurred the collection return item is sent to the country collection department instead. This department returns the item to the bank's client together with reasons for non-payment.

### Interest Delays

While the bank gives immediate credit for deposits of items payable out of town, it does not have the use of them for loaning purposes until the time required for collection has elapsed. If the depositor of such items is receiving interest on his account, the bank obviously cannot include them in his interest-bearing balance. To make sure they are not included, a clerk from the transit department inspects the incoming remittance letters, and indicates the "interest delay" on each. This process consists simply in placing a stamp on

the letter showing the amount which is not immediately available for use by the bank and the number of days required to collect it. When the letter passes to the bookkeeper for posting, as it does presently, the whole amount is posted to the credit of the sender's account while the interest delay is deducted in arriving at the balance upon which interest is computed.

### Disposition of Debit and Credit Items

The debit or cash items contained in the letters are sorted and distributed just as are similar items in the receiving teller's work. Instead of sending the clearing house items contained in the morning mail to the assembly rack department, the mail teller's department performs the assembling process itself in order to prepare as many items as possible for clearing on the day of receipt.

Remittance letters which contain credits for more than one bank are replaced by departmental credit tickets, one for each bank which is to be credited. After the letters have been marked for interest delay they are sent to the bookkeepers who post them to the credit of the customers' accounts. The letters then are returned to the mail teller's department where they are used as the basis for letters acknowledging the receipt of the remittances. These letters are prepared in duplicate, and in case one customer has sent a remittance for the credit of another, a third copy of the letter is made for the depositor whose account was credited.

To eliminate so far as possible errors in advising, the letters of advice are proved against the remittance letters. The original advice is then sent to the outgoing mail department to be forwarded to the remitter. The duplicate letter is sent to the statement clerks in the customers bookkeeping department. It will be recalled that the ledger bookkeepers in that department have posted their credits from the remit-

tance letters. The statement clerks use the duplicate letters of advice in posting credits to their statements of the remitters' accounts. At the close of the day the ledger bookkeepers and the statement clerks check their work against each other. Proof of the accuracy both of the entries and of the letters of advice is thus obtained.

### **Special Instructions Force**

A special force in the mail teller's department cares for all the instructions received from depositors. These are of two kinds: the standing orders, and the special instructions. The standing orders consist of requests to advise a concern's home office of deposits received from its branches, to change addresses in mailing letters of advice, to wire advices in connection with certain deposits, and a wide variety of similar directions. When the bank receives a request to furnish special service of this nature the mail teller is advised of the order and his is the responsibility of handling each transaction in accordance with the customer's wishes. These standing instructions are filed in a tickler and are kept up to date by the clerks who are in charge of this phase of the mail. Special instructions are those which pertain to a single letter or to only one or more items in a letter. They consist principally of requests to wire the remitter concerning the fate of an item in its passage through the collection process. The instructions force examines each letter and makes sure that each special and standing order has been strictly followed. The remittance letters are then forwarded to the general files of the bank.

### **Mail Teller's Proof**

The proof of the day's work of the mail teller's department is one of the most elaborate in the bank. It illustrates the "batch," or "block," system of preparing proofs so well adapted

to use by bank departments in proving and recording their day's work. At the same time a description of the mail teller's proof serves to bring out the fundamental principles of the batch system. This proof is, therefore, given somewhat in detail.

The system of proving can be understood only by keeping clearly in mind the division of labor within the department, since the proofs follow the lines or blocks of these divisions. The batch is the unit of work. It consists of an arbitrary number of remittance letters together with their contents. A certain number of batches make up a section. A section consists of all the cash mail received for the credit of a definite group of depositors the accounts of which are kept in one or more of the ledgers in the bookkeeping department. The five sections make up a division of the mail, of which there are three—the night mail, the morning mail, and the afternoon mail. These three divisions are combined to form the largest unit—the day's mail.

### **Rack Proof**

The construction of the rack proof begins with the batch proof which has already been described (Form 2, page 22). As the batches are proved and sent away, the batch proof sheets are retained as a record of the work. When all the work for a given rack has been completed the proof clerk for that rack prepares a rack proof.

### **Proof of Division**

The rack proofs are combined into three divisional proofs. The first one of these records the work of the night mail, the second one adds the results of the morning mail; and the third one gives the results of the afternoon mail. On the debit side of the proof of the division there are entered in the first column the total letters of each of the five racks, the

amounts which other banks clearing through this bank have sent to the mail teller to be cleared (only on the morning division of the proof), and the items which other tellers of the bank have sent to be cleared (only on the morning division) The columns following to the right contain the distribution of the items handled by each rack and of those received from the tellers and banks which clear through this bank The total of the letter column proves with the total of the distribution columns The credit side of the proof shows the distribution of the credits

- 1 As made to depositors' accounts contained in the various ledgers
- 2 As made to other departments of the bank for items which they have sent to the mail teller
- 3 As made to the Collection Ledger account for remittances received in payment of collections

The total of these columns must prove with the total letters on the other side of the proof

### **Mail Teller's Daily Proof**

The mail teller's daily proof is a combination of the divisional proofs On the credit side under the title "credit journal" are shown the total credits sent to the bookkeepers Credit is also given to each teller and department for cash items which they have sent to the mail teller's department On the debit side is shown the distribution of the debit items which the mail teller has handled during the day as follows

- 1 The total clearing house, to the first teller
- 2 The country items, to the transit department, except in the afternoon when small countries are charged to the city collection or fifth teller's department to be kept overnight
- 3 The checks drawn on the bank itself, to the check desk

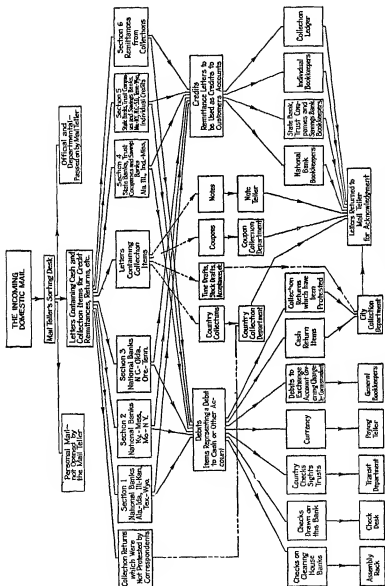
- 4 The currency, to the first teller
- 5 The cash return items, protest fees, sights, trusts, small countries, hold-overs, etc., to the city collection department
- 6 Exchange, to the check desk

The mail teller's daily proof (Form 5) completed in this manner becomes a permanent record of the department and

FOURTH TELLER'S PROOF <i>Dec. 31-1921</i>					
<b>A. M. Transit Dept.</b>			<b>Credit Journal</b>		
Check Clerk No. 8,		2,762,430.67		41,467,314.56	
Clearing House 1st Teller,		9,316,892.69	Int. from 1st Teller,		
Paid to 1st Teller,		20,673,033.57			
" 2nd "			" 2nd "		
" 3rd "			" 3rd "	804,382.03	
" 5th "			" 5th "	794,679.07	
Sight Drafts,		4,874,439.32	" Foreign Dept.	1,400,230.48	
Cash Items,		2,202.75			
<b>Total,</b>		<u>37,630,999.32</u>	<b>Total,</b>	<u>44,466,606.14</u>	
<b>P. M. Transit Dept.</b>					
Check Clerk No. 8		645,473.68	Int. from 1st Teller		
Clearing House Exchanges		1,664,769.73			
Paid to 1st Teller		3,538,586.67	2nd "		
" 2nd "			" 3rd "		
" 3rd "			" 5th "		
" 5th "					
Large Sights		419,436.06			
Small "		459,283.69			
Transfer to Transit Dept.		107,574.05			
Cash Items,		472.94			
<b>Total</b>		<u>44,466,606.14</u>	<b>Total</b>	<u>44,466,606.14</u>	

Form 5 Fourth, or Mail, Teller's Daily Proof. (Size 9 x 9 1/2)

is placed in the binder with the proofs of the work of preceding days. The disposition of the cash and collection mail items is shown graphically on Form 6



Form 6 Chart Showing Disposition of Cash and Collection Mail Items Received by Mail Teller's Department

Broken lines represent bills covering exchange charges deducted by correspondents and sent through the collection ledger rather than credited to the customer's deposit account when such bills represent collections sent out on a remittance basis.



### The Work of the Foreign Tellers—Receiving Section

A section of the foreign teller's department receives and acknowledges all deposits coming over the window for credit of foreign depositors. The work of this section is not sufficiently distinctive from that of the domestic receiving teller to warrant detailed treatment here, hence only the important differences will be noted.

The term "foreign" is applied to the foreign tellers by virtue of the class of customers they serve, rather than because of the items which they receive. In fact, the items which these tellers receive for credit to foreign accounts are not only domestic in character, but they are local as well.

The custom of charging items back to depositors' accounts is, no doubt, not so firmly established in foreign countries as in the United States. Again, foreign depositors very frequently draw cable transfers against their deposits on the day of receipt. For these reasons the bank pursues a policy of assuring itself absolutely that an item will be collected before it advises a foreign depositor of a credit to his account.

Several devices are used by the bank to assure itself that an item will be collected before the funds are placed at the disposal of the depositor. In the first place, as indicated above, only the money of the United States and checks payable in New York City are accepted. No voucher check is received for the reason that the act of a bank in paying such a check may be construed in foreign countries as a guarantee on the part of the paying bank that all conditions mentioned in the voucher have been complied with. Again each check must be drawn to the order of the receiving bank or it must bear a well-known indorsement. In case a check of considerable size drawn upon a neighboring bank is presented, it is sent to the drawee bank for certification before it is credited to the account of the depositor. Checks upon the receiving bank itself are made certain of payment by

having the bookkeepers place a "hold" against the account of the drawee until the check can reach the bookkeepers in the regular way and be charged. In this manner the bank avoids misunderstandings and complications by practically collecting each item before the deposit is acknowledged.

### **Standing and Special Instructions**

The prevalence of standing and special instructions which the bank must follow in accepting a deposit is worthy of note in connection with the foreign work. The foreign customer is at a considerable distance from the bank and conditions in the foreign exchange market are always such that he may desire to draw against a deposit by cable immediately after it is made. To meet these conditions the receiving bank is often called upon to acknowledge receipt of a deposit by cable. As in the work of the mail teller, the foreign receiving teller has on file a variety of standing orders with which he must be familiar and any special instructions pertaining to a given deposit must be faithfully followed. The situation is such that practically each transaction must be handled individually.

### **Credit Advice**

Instead of making an entry in a pass book or signing a duplicate deposit slip, as does the domestic receiving teller, the foreign receiving teller prepares a special "credit advice" (Form 7). This is written on forms, four to a set, bearing the same number. The first copy is for the depositor, in case he is a party other than the one who is to receive credit, the second is mailed to the foreign customer whose account is credited, the third is an office copy, and the fourth a credit ticket for the bookkeepers. In addition to the credit advices the bank may be called upon to sign a special form of receipt or mail a special letter of advice concerning the deposit. Requests for the latter type of service are complied with only

after care has been taken on the part of the bank to ascertain what its liability may be for such an act. In fact, all this special care and attention which the bank gives to preparing and checking advices of the receipts of foreign deposits are due to the fact that a foreign depositor cannot always be expected to construe a bank's responsibility for the instruments

ADVICE OF CREDIT	<b>The National City Bank of New York</b>	
	FOREIGN TELLERS	
	<b>ORIGINAL</b>	New York, MARCH 28, 1921.
	----- ROTTERDAMSCH E BANKVEREENIGING -----	
	----- AMSTERDAM, HOLLAND. -----	
	ADVICE No R ----- 22908 -----	Your account has credit
	For ----- THIRTY THOUSAND DOLLARS ----- \$ 30,000 00	
	Deposited by ----- HALLGARTEN & CO ----- N.Y. CITY. -----	
	For account of ----- YOURSELVES ----- value 3/28/21.	
	THE NATIONAL CITY BANK OF NEW YORK	
By <u>William Jones</u>		

Form 7. Foreign Teller's Credit Advice (Size 7 x 4.)

which bear its signature in the same way as does a domestic customer

### Summary of the Receiving Operations

At the close of the day the receiving departments of the bank have a clean slate. Whatever work has come to them has been examined, recorded, and passed on for other phases of the banking process. It is well at this point to summarize the results accomplished in the receiving process.

These results are two. first, the bank has come into possession of certain raw material for further banking processes; second, bank credit in the form of rights to draw upon the bank has been created.

The receiving operations of a bank are essentially the results of an exchange between the bank and its depositors. In exchange for deposits the bank grants its customers the right to draw drafts (checks, bank drafts, etc.) against it to the extent of their deposits. In other words, the deposit transaction is one involving the exchange of bank credit for cash or its commonly accepted equivalents. Through the deposit operations bank credit is built up.

These operations impose upon the bank two obligations. First, the "cash" which the bank has received does not consist of money in most cases. It consists rather of checks, drafts, etc., which are payable at the places of business of more or less distant drawees. In order to use these funds for making loans, meeting depositors' checks, building up reserves, etc., it is necessary that the receiving bank collect them from the drawee.

Second, the receiving bank has assumed the obligation of honoring at all times authentic checks drawn upon it. In exchanging cash or its equivalents for bank credit the depositor can be expected to do so only if he feels absolutely sure that his check against the bank will be more useful to him than the items which he proposes to exchange for it. The usefulness of a check depends upon its acceptability. Acceptability of a check depends upon the faith which the one to whom it is offered has in the ease and certainty of its being converted into cash. The certainty of a check being converted into cash is established by the unvarying policy of the bank upon which it is drawn of standing ready to honor all checks drawn upon it by its depositors who maintain sufficient balances with the bank to cover such checks as they are presented for payment. Thus the second obligation of a bank arises. It is that of standing ready, both with funds and with assessable banking machinery, to meet the instruments drawn on it by its depositors.

## CHAPTER III

### THE PAYING OPERATIONS

#### Nature of Paying Operations

The term "paying operations" includes that part of the work of a bank which is performed by the paying or first teller's department and others closely related to it. In general these operations consist of two fundamental parts. (1) maintaining and caring for an adequate supply of cash, and (2) paying out the cash of the bank, i.e., cashing checks and making other similar payments for customers' accounts. In this connection the term "cash," as used here to denote money or circulating media, must not be confused with the term "cash" as it is employed frequently to denote not only money but also checks and other items which are commonly accepted as equivalent to money. The latter, for the sake of clearness will be termed "cash items" whenever necessity occurs for referring to them.

#### Relation to Receiving Operations

The paying operations are closely related to the receiving operations. In the first place the cash which the receiving operations have brought into the bank goes directly to the paying, or first, teller's department and it becomes in part the material upon which this department works. In the second place the actual disbursements which are comprised in the term "paying operations" are for the purpose of honoring drawings made against credits which have arisen from the receiving operations. The two functions of the paying departments thus arise largely from the activities of the receiving departments.

### Organization

The specific operations included in the term "paying" consist of

- 1 Counting and testing the cash receipts of the bank
- 2 Maintaining and caring for this cash
- 3 Paying checks, clearing house balances, making currency shipments, etc
- 4 Certifying checks
- 5 Attending to the pay-roll of the bank and other expense payments

The organization of a bank for this work depends entirely upon the volume and character of each of these specific operations. In a large down-town New York bank the task of counting, verifying, and preparing money for storage is a particularly heavy one, and at the same time the work is highly specialized. This operation is performed by a money department. The certification of checks, while closely related to the process of actually paying them, requires a specialized type of service. Owing to the needs of stock brokers who use this type of instrument to settle their obligations the work is heavy enough to occupy the time and attention of a certification department. The work of paying certain petty expenses of the bank, as well as handling the pay-roll, is important enough in volume and in scope to occupy the attention of a petty cashier. These three departments relieve the parent department—the paying teller's—of much of the work which would otherwise fall to its lot. The parent department, then, performs the basic operations of maintaining an adequate supply of cash and making payments to meet the conveniences and the demands of customers.

### Counting Cash

Of the various processes performed by a bank the handling of cash requires the greatest care. In the first place the ready

negotiability of cash makes it subject to the designs of dishonest persons both from without and from within the bank. Second, and more important still, the difficulty of tracing cash once it has been passed from one person to another, or once it has passed from within the confines of a small lot into those of a larger one, renders the correction of errors practically impossible.

For these reasons a bank takes every possible precaution to prevent errors in handling cash and to safeguard its money supply. Only trusted employees have access to the cash. Each teller has his individual steel cage within which he transacts his day's business and to which other employees of the bank are denied admission. Whenever cash is transferred from one department to another each party to the transfer signs a memorandum for the records of the other. Whenever in the course of the day's business it happens that a department other than the paying teller's comes into the possession of cash, that department is required to forward the larger bills to the paying teller immediately. As a general rule no cash is held overnight except by the paying teller. Each teller or employee through whose hands cash passes prepares a separate proof thereof. Finally, the supply is kept in vaults which are as nearly fire- and burglar-proof as it is possible to construct them. Inside the bank watchmen are kept constantly on duty. In New York City the protection which banks enjoy extends even to the streets of the financial district, which, by police regulation, are made virtually inaccessible to all persons having a criminal record.

### Money Department

The money department is a specialized organization for counting and verifying the cash of the bank. The money which comes into the paying teller's hands, with the exception of some few small packages of very large bills which may be

readily verified by the teller himself, is passed to the money teller against his receipt for it. The work of the money teller's department is to count the money, examine it for genuineness and for currentness, and to prepare it for storage in the bank's vault.

The money teller takes the money for his day's work in a covered truck into a special cage which is inaccessible to all employees of the bank other than those of his own department. His force of employees is divided into crews, each crew being responsible for a definite amount of work assigned and charged to it. Two persons in each section count and verify the money which has been assigned to them, they must prove against each other and against the amount which has been charged to them. After counting the money, which they do by hand excepting in the case of minor coins, the counters wrap the coins, separate the bills into packages of standard size, and place their names on each package or roll. These precautions minimize the chance for errors and fix the responsibility for the work of the department directly upon those immediately concerned with each portion of it.

### Scrutiny for Genuineness and Currentness

The counters act as a court of final resort in passing upon the genuineness and currentness of the money which comes into the bank. A part of the money has already been carefully examined as a necessary part of the work of the tellers who first come into possession of it. The bulk of the cash, however, is received from customers subject to count and examination and, if any defects such as inaccurate count, worn or mutilated condition of coins, or counterfeits, are found the understanding with the customer is that the amount in question may be charged back to his account. The money-counters, accordingly, are constantly on the lookout for all these defects.



### Counterfeit Money

It is not the purpose of the present discussion to describe methods of detecting counterfeit money. This is largely a matter of judgment which tellers acquire by long experience in handling cash. An experienced teller comes to know from the feeling, appearance, and weight of a piece of money whether it is genuine or not. To supplement his knowledge each teller has a copy of the *Counterfeit Detector*, a periodical publication giving the description of each known counterfeit issue which has been reported by banks, the secret service, and others interested in detecting counterfeit money. Whenever a piece of counterfeit money is discovered, the bank charges it back to the customer who presented it, stamps it "counterfeit," and turns it over to the secret service department of the government.

### Raised Money

Raised money is met with much more frequently than counterfeit. The detection of this irregularity is, however, relatively a simple process. In sorting the money the bills are grouped by separate kinds and denominations. Since a raised note bears the engraving of a lower issue rather than that of the one it purports to be, it is readily detected as an impostor in the bundle of notes of a higher denomination.

### Mutilated and Worn Money

All mutilated and worn bills and coins are laid aside by the counters to be sent away and replaced by new ones. Inasmuch as the sources of new currency are readily accessible it is the practice of the bank to carry only new money in stock and to make its payments only in crisp bills and full-weight coins. Redemption of uncurrent money usually involves simply an exchange of the uncurrent bills or coins for new ones at the near-by sub-treasury or federal reserve bank with-

out any considerable expense, hence the bank performs this function gratuitously as a service for its customers. Mutilated and light gold coins, however, cannot be redeemed at face value. They must be sold for bullion. Therefore the bank handles them for the account of the depositor. Light silver and all worn and mutilated paper currency are redeemed by the government at face value in most cases. Whenever a piece of paper money is so mutilated that less than three-fifths, but more than two-fifths, of the bill remains, that bill is redeemed by the government at half its face value. Mutilated bills of which less than two-fifths remain are worthless. Provision is made by the government, however, to the effect that any fragment of paper money will be redeemed at its face value provided the holder furnishes an affidavit stating that the remaining portion has been wholly destroyed and also stating the means by which it was destroyed.

The local federal reserve bank redeems coins, legal tender notes, and federal reserve notes. The Treasurer of the United States attends to redeeming national bank notes, and formerly the bank always sent them to him for this purpose. Recently, however, the local sub-treasury<sup>1</sup> has adopted the policy of receiving these notes as payment against the 5 per cent fund which banks of issue are required to maintain at the treasury for the purpose of redeeming their bank notes. In accordance with this policy the bank uses these notes almost exclusively for making payments for account of its own 5 per cent fund, as well as that of its customers who ask the bank to make such payments for their accounts.

### Preparation of Money for Storing

After the money has been counted and verified it is prepared for storing. To facilitate the work of storing and that of counting and handling the money in the future, the money

<sup>1</sup> While this book was in process of preparation the local sub treasury was closed and its functions assumed by the federal reserve bank.

is sorted as to kinds and denominations and put up in standard size packages which become the storage units for the money of the bank <sup>2</sup>

Preparing the money for storage completes this part of the work. At the close of the day a proof is prepared and the money is placed in the vault for use by the paying teller.

### Paying or First Teller's Department

In the bank where the volume of the work justifies the organization of specialized money, petty cash, and certification departments, the functions of the paying, or first, teller's department are narrowed and specialized so as to include the following:

- 1 To take charge of all cash of the bank
- 2 To keep the bank's cash
- 3 To provide for an adequate supply of money for the bank's needs
- 4 To pay checks
- 5 To ship currency to customers.
- 6 To sell bullion
- 7 To settle clearing house balances
- 8 To record and prove the cash of the bank

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<sup>2</sup> As to kinds, the paper money is sorted into gold certificates, silver certificates, legal tender notes, federal reserve notes, federal reserve bank notes, and national bank notes. The packages are then made up as follows:

\$100 bills are strapped in packages of \$2,500	
50 " " " " " "	1,000
20 " " " " " "	1,000
10 " " " " " "	500
5 " " " " " "	250
2 " " " " " "	50
1 " " " " " "	50

The minor silver coins are put through an accounting and wrapping machine which prepares them as follows:

\$ 50 coins are wrapped in rolls of \$10.00	
25 " " " " " "	10.00
10 " " " " " "	5.00
05 " " " " " "	2.00
01 " " " " " "	50

Three separate divisions of the paying teller's work are readily suggested from the nature of the operations. First, there is the custodianship of the cash, second, the work of making payments, third, the clerical work of recording, proving, and disposing of the items. Of these three, the second one is the ruling factor in influencing the size of the department.

Just as the volume and character of the window work of the receiving teller of the Wall Street bank is characterized by heaviness in money value and by lightness as to the number of items, so the work of making window payments also consists of relatively few but large transactions. The greater volume of checks which depositors draw upon a bank of this type are settled either through the clearing house or by deposit through the mail teller's or through the receiving teller's department. Under such circumstances the organization of the department for the window work consists of but one teller and a small number of assistant paying tellers. The clerical work of proving and distributing the checks which are paid at the windows is also light, corresponding to the small volume of work at the windows. A small clerical force completes the subordinate organization. The paying teller himself is the custodian of the bank's cash and he is in control of the work of the department.

### **Maintaining Supply of Cash**

The most important duty of the paying teller consists of maintaining and keeping the bank's supply of cash. This work involves first, seeing that the bank has a sufficient supply of cash on hand and, second, storing and caring for the cash which is held. The first of these duties implies (1) a pre-determined ratio of cash reserve to deposit liability, (2) replenishment of the supply, and (3) disposition of surplus money.

### Replenishment of Supply

The paying teller is charged with the duty of keeping a watch over the bank's cash which he must replenish if the supply shows tendencies towards running low either in total amount or in supply of the various kinds and denominations. The first of these duties is performed by the teller acting upon the orders of the cashier of the bank. The latter function is properly that of the paying teller in his capacity as custodian of the bank's cash and he acts upon his own initiative in performing it. From the point of view of the teller's department alone, the latter function is the more important in the sense that it requires a considerable portion of the time and attention given to the work of the department.

### Disposition of Surplus Money

The bank obtains its supply of money from three sources. First, there are the daily receipts which come from customers of the bank. These receipts consist of the cash deposits received by the various tellers, payments of loans, discounts, collections, and miscellaneous banking services, and currency shipments which come directly to the paying teller from correspondent banks. This source of supply, while considerable, is insufficient to meet the bank's daily needs for ready money. Second, the bank obtains cash from the United States Treasury where it exchanges mutilated and worn money for new, or kinds and denominations of which it has an excess for those of which it has need. The third source is the local federal reserve bank where, in addition to being able to exchange kinds and denominations of money, the bank is able to supply its needs for additional supplies of money. Thus it does by drawing against its deposit balance with that bank.

Surplus money, in the banking sense, may be either worn, mutilated, or unwanted money, or it may be money in excess of the bank's needs in amount. Surpluses of the first type

are disposed of by sending them to the source for redemption, exchange, etc., as has already been indicated. When a bank has accumulated a surplus of the second type it simply makes an addition to its lawful reserve by depositing the excess amount with the federal reserve bank.

### **Supply of Money for Other Departments**

In addition to keeping watch over the aggregate supply of cash held by the bank, it is also the duty of the paying teller to supply all other tellers and departments of the bank with whatever supplies of domestic money they may need to transact their day's business. As a general rule the paying teller's department is the only one in the bank which is permitted to keep cash overnight. Accordingly at the close of each day he receives the net cash resulting from the other operations of the bank. At the beginning of the next day he replenishes those departments which may be in need of funds with a supply sufficient for that day's requirements. Should need for more cash arise in the various departments, they make out requisitions and obtain additional supplies from the paying teller.

### **Storing Cash**

The cash of the bank comes to the paying teller from the money department in standard size packages. To facilitate counting, proving, and keeping record of the adequacy of the supply, it is stored by kinds and denominations. Furthermore the vault is divided into three sections: (1) the reserve section, (2) the paying teller's section, and (3) the window teller's section. The reserve section contains cash in the hands of the cashier of the bank and, as its name indicates, is a sort of safety fund to meet unusual demands. The second section of the vault contains the main cash supply of the bank or, one might say, the working cash. The third section con-

tains the cash which is to be used by the assistant paying tellers to make window payments in cashing checks

Each day a rough proof is prepared showing the kinds and denominations of money contained in the stock of working cash. These figures must agree with those appearing in the paying teller's daily proof to be described subsequently. At the close of the day a statement is also prepared for the cashier of the bank showing the total amounts of the various kinds and denominations of money on hand and the amount contained in each of the three vault sections.

### Cashing Checks

The work of cashing checks is performed by assistant paying tellers, aided by the paying teller himself, as the needs of the day may require. In preparing for this work the tellers take their supply of cash from the vaults and arrange it in their individual cages in a manner which facilitates proving and paying. Bills are arranged in racks and drawers by kinds and denominations. The larger denominations are placed in the more inaccessible places to prevent their being paid out by mistake for smaller ones. Gold and silver coins are arranged in trays by denominations. The teller is thus prepared to handle his line of customers without the necessity of frequent trips to the vault.

The process of cashing a check is one which requires the utmost care on the part of the man at the window. Other departments of the bank deal more or less with book entries which may be adjusted without loss to the bank. The receiving teller, for example, merely gives credit for the items he receives. Should errors arise he can correct them by recall or a revision of the credit which he has made. The paying teller, however, having parted with cash cannot charge anything back to a depositor's account, for the nature of cash is such that it is practically impossible to identify the money

once it has been paid out and to furnish convincing evidence to the customer that an error has actually been made. Direct financial loss, therefore, is likely to result from any error made by the paying teller

Moreover, the prestige of the bank is in the hands of the teller each time he cashes a check. First, the interests of the drawer of the check, who in the majority of cases is a customer of the bank, are to be safeguarded. The teller is accordingly on the alert to avoid paying forged, postdated, antedated, and otherwise irregular checks, also those against which the drawer has filed stop-payment orders. Another situation which calls for care in protecting the customer's interests arises in connection with watching overdrafts. Should the teller in his zeal to protect the bank make frequent inquiries of the bookkeepers regarding the state of the balance of a customer who habitually keeps adequate balances, it is obvious that the reputation of such a customer may be injured. Second, the teller has the interests and the convenience of the one who presents the check to safeguard. The work at the window, therefore, requires the greatest amount of tact.

The work is made easier and simpler by an intimate knowledge of the various customers who come to the window. The large majority of the transactions are handled in a regular manner and without any particular difficulty. In general the teller verifies the indorsement of the check, sees that no stop-orders are on file against it, and examines the check for signature, date, and filling before he pays it. In many cases he is obliged to examine further into the identity of the one who presents the check to be cashed or to ascertain the adequacy of the balance of the drawer.

### Indorsement

Taking in their regular order the factors which must be considered before a check is cashed, first comes the matter



of indorsement. Checks are made payable either to order or to bearer. Each check payable to order is required to be indorsed by the person who presents it. Checks which are drawn payable to "bearer," or to "cash," or in some manner which makes them negotiable by delivery only, are generally indorsed also in order that the drawer of the check may use it as a receipt after it has been returned to him. In cases where a check payable to bearer is presented by a well-known customer, indorsement may be waived. For his own information it is common for the paying teller to write a memorandum on the back of the check covering any particulars of the transaction which he may wish to keep in mind.

### Stop-Payment Orders

After a check has been drawn, the drawer may wish to prevent the bank from paying it. Many cases arise in which the status of a check becomes so changed between the time when it is drawn and the time when it is presented to the drawee bank for payment that a hardship would be worked against the drawer were there no means available for stopping the payment of the customer's check. A customer who wishes to stop payment upon a check files with the drawee bank a notice called a "stop-payment order." These notices are handled by the check clerk whose duty it is to pass upon all checks before they are charged to the accounts of depositors on the books of the bank, and in the work of most of the departments a stop-payment need not be enforced until the check reaches the check desk. The paying teller, however, is to pay cash for checks, hence he sees that no stop-payment orders are in effect against checks before he pays them. To meet this need all notices of stop-payment come to the attention of the paying tellers, and those concerning checks which these tellers are likely to be called upon to pay are entered

on their list of stop-orders. Most of these orders are memorized by the tellers, but the list is kept accessible for reference should need arise. The list is kept up to date for only a few days immediately preceding the current day. As a matter of regular business procedure all checks which are more than two or three days old are regularly referred to the bookkeepers before payment is made, and stop-payments on such checks would receive attention in this manner.

### Signatures

The bank in guarding carefully against the payment of forged checks safeguards its own interests as well as those of its depositors. By practice the paying teller comes to know the signatures of those customers whose checks come to him regularly. In cases of doubt as to the genuineness of the signature, reference is made to a signature file which the paying teller has in his cage. This includes the signatures of all domestic accounts.

### Date

The bank is constantly on its guard against paying both postdated and stale checks. To pay a postdated check would prevent the maker from exercising the right to stop payment. While the duty of a bank to honor a check is not affected by the age of the check, at least within the period set by the statute of limitations, the older a check becomes the more danger there is that some reason which would justify non-payment has arisen. It is the practice of the bank, therefore, to refuse to pay postdated checks and to refer stale checks to the bookkeepers, and possibly to the makers, before they are honored.

### Irregularities

Irregularities in the instrument, such as change in or lack of date, sum payable, time or place of payment, number or

relation of parties, the medium in which payment is to be made, or want of agreement between figures and words in expressing the amount of the instrument, are carefully looked for before the check is paid. In case such an irregularity is discovered and no satisfactory explanation or adjustment is forthcoming, payment of the check is refused.

### Insufficient Funds

It is the duty of the paying teller to guard against paying all checks for which the drawer has not sufficient funds on deposit. The most satisfactory preparation of the paying teller for this work consists in a knowledge of the kind of account each depositor keeps. While the overdrawing of a depositor's account must be guarded against, too much zeal on the part of the teller in inquiring of the bookkeeper regarding the status of the account is likely to be regarded as a reflection on the credit of the depositor. By knowing the accounts with which he comes in contact, the teller is able to avoid doing this. The teller, however, considers it best to make sure of the status of the balance whenever there is doubt regarding an account. In a situation of this kind he refers the question of the adequacy of the customer's balance to the bookkeepers by means of the telautograph. Such an investigation, of course, is conducted quietly and quite unknown to the person outside the window.

### Identification

In the United States a bank is liable to its depositor in case it pays a check drawn against his account to an unauthorized payee. Were there no legal liability, however, the attitude of the bank as to identification would be unchanged. The bank which desires to give its customers the highest type of service exercises greatest care in making payments on a depositor's order. Thus even in the case of an item which

is made payable to bearer, where the bank could legally make payment to whomsoever might present the item, it takes steps to establish the identity of the one who demands payment before it makes payment. The paying teller is personally acquainted with the majority of those who present checks at his window. Often, however, he deems it necessary to require specific identification of the holder.

Various means are used to establish a person's identity. One of the best is to have the stranger secure the indorsement of a depositor of the bank. A good plan which is frequently used is that under which the maker of an instrument guarantees the indorsement on it. In other cases out-of-town correspondents send written signatures of the payee of their drafts to the drawee bank by a letter of advice which is received before the draft is presented for payment. In case of small items or foreign items, the one who presents them for payment usually has on his person letters, passports, lodge cards, etc., which may safely be accepted as establishing his identity. The paying teller's first duty, however, is to guard the bank's cash, and in cases of reasonable doubt as to identity he is obliged to decline payment.

### **Payment of Checks Drawn upon Other Banks**

The foregoing precautions apply particularly to the operation of paying a check which is drawn upon the paying bank itself. The bank is also called upon to cash checks which are drawn upon other banks as well. In cases of this sort it is impossible for the paying teller to satisfy himself in many important particulars as to the collectibility of the check. He cannot be expected to know the signature of the drawer. Information regarding stop-payments, adequacy of balance, etc., is not available to him. A check of this sort is taken practically on the standing of the one who presents it. In general, such checks are cashed only for persons exceptionally

well known to the bank or when such checks bear the indorsement of a customer or an officer of the bank

### **Making Payment**

After having scrutinized the check and decided that it is regular in every respect, the paying teller makes payment. In this apparently simple act there is a real opportunity for a bank to cater to the convenience of its customers. Requests for specific kinds and denominations of money are based upon the important needs of the customer and the bank makes it a matter of policy to comply with such requests. When a customer needs large quantities of different kinds and denominations of money he is asked to prepare a special requisition which he presents with the check to be cashed.

### **Disposition of Items Received**

The operations at the window result in an accumulation of checks for which cash has been given. These checks are proved and sorted into two groups: (1) those drawn upon the bank itself, and (2) those drawn upon other banks. The checks of the latter group are entered in a memorandum book which shows the name of the drawee bank, the indorser, and the amount of each check. The checks are then disposed of by charging and sending those drawn upon the bank itself to the check desk and all others, because of the small amount involved, to the city collection department.

### **Sundry Payments**

In addition to the cashing of checks certain other disbursements of currency for customers are made by the paying teller's department. As an example of this, the bank often receives from out-of-town national banks requests to make payment to the United States Sub-Treasury for the account of the 5 per cent redemption fund which these latter banks are required to

maintain against their outstanding circulation. To make a payment of this sort the bank uses the mutilated national bank notes which it has received. These are charged to the account of the out-of-town bank and sent in the proper amount to the United States Sub-Treasury of New York for credit to the fund of that bank. Thus the double object of effecting the redemption of the mutilated bank notes and of filling the customer's order for a payment to the credit of his 5 per cent redemption fund is accomplished in the same transaction.

### Currency Shipments

Frequently customers request the bank to make shipments of currency to themselves or to others for their accounts. These requests may be for shipment of gold to foreign countries made because of developments in the foreign exchange market, or they may be for shipment of specific kinds and denominations of money to fill the needs of domestic banks. Some of these latter banks have standing orders on file for periodical shipments to be made against their accounts. All letters requesting shipment of money are sent by the paying teller to the bookkeeper's and signature departments for balance and verification of signatures, and on their return a charge ticket is made out against the account. The money is then made up for shipment and turned over to a special messenger who, with his assistant, puts it up in sealed packages and delivers it to the express company or post-office against receipt. Shipments to foreign countries require that the regulations of the United States and foreign governments, as well as those of the steamship company, in regard to documents and other formalities be complied with. It is the duty of the special messenger to attend to all these details. An affidavit covering every shipment of currency is filled out and signed by the messenger and his assistant who handle it. Two advices and a special request for acknowledgment are

prepared. One advice is enclosed in the shipment, while the other, together with the acknowledgment form, is forwarded under separate cover by mail.

### **Sale of Gold Bars**

What might be termed a third type of sundry payment consists of the sale of gold bars and bullion to the customers of the bank who desire to use such material in manufacturing jewelry, dental supplies, etc., or to banks which desire to satisfy similar demands from their customers. The bank performs this function as a service to its customers, making the sale at the cost price of the metal. Bullion for this purpose is obtained from the local United States assay office.

### **Settlement of Clearing House Balances**

Formerly the system of settling clearing house balances at the New York Clearing House was such that actual money had to be taken to or from the clearing house by a member bank, according as it had a debit or a credit balance resulting from a given day's clearing. Under the present system, however, the settling of clearing house balances is effected merely by book entries. The paying teller attends to the clearing house transactions in the following manner. He is charged with the amount of exchanges sent to the clearing house by the mail teller and this figure then becomes a debit upon his records. The amount received from the clearing house is credited to him and in turn charged to the check clerk. This amount appears on the paying teller's record as a credit. If the clearing house balance is a credit balance, the amount is charged to the Federal Reserve Bank of New York under the heading "Lawful Reserve with the Federal Reserve Bank of New York" and the paying teller credits himself for the amount just as he would in recording an ordinary payment. In case the clearing house balance is a debit balance, the entry

is reversed and the entry to Lawful Reserve with the Federal Reserve Bank of New York appears on the debit side of the paying teller's records

### **Paying Teller's Proof**

At the close of the day's business a proof is prepared which is in essence a record of the bank's cash. The exchanges which have been taken to the clearing house and the net amounts received from the other tellers of the bank during the day are added to the balance of the previous day. A total of these amounts gives the total debits to cash for the day. On the credit side of the proof appear the amounts of exchanges received from the clearing house, the checks upon the bank itself which have been paid during the day, and the net amounts sent to the other tellers of the bank. The difference between these two sides of the cash account represents the balance for the day, and the amount is entered upon the credit side of the proof. A third section shows the details of the cash on hand by kinds, by vault numbers, and by the vault sections of the cashier, paying teller, and assistant paying tellers. This proof is filed in a binder and becomes a permanent record of the bank.

### **The Petty Cashier**

The work of preparing the pay-roll of the bank generally devolves upon the paying teller's department. As the bank grows and this work becomes proportionately heavy, a special clerk called the petty cashier is assigned to handle it. In addition to the work of preparing the pay-roll, bonus, allowance, and salary advance payments to employees, the petty cashier also has the work of purchasing and distributing postage and revenue stamps and of keeping the petty cash fund and making the sundry small payments which are to come out of it.



### **Pay-Roll**

The methods used by a bank in handling these transactions do not differ materially from those used by other business concerns. A list containing the numbers assigned to each of the employees and the amount of pay which each is to receive comes to the petty cashier from the organization department some few days before the regular semimonthly pay-day. Along with this list comes a check drawn to the order of the petty cashier for the total of the pay-roll. This check is cashed and the pay envelopes made up and delivered to the division heads of the bank against receipt. As each employee receives his pay he verifies the amount and signs a receipt. All uncalled for envelopes are returned to the petty cashier who attends to delivering these over his window. The auditors of the bank and the general bookkeepers receive a copy of the pay-roll sheets, also the receipts which were signed by the employees as they received their salaries. From these records the auditors are enabled to check the work of the petty cashier.

### **Petty Cash and Stamps**

To care for the petty payments of cash a special fund of convenient size is made up and put in the hands of the petty cashier. Upon proper authorization he makes payments out of this fund, charging the proper accounts on his records. These records are audited at intervals, say weekly, and a reimbursement check is issued to the petty cashier. Postage and revenue stamps are purchased at the source by the petty cashier. The various departments of the bank obtain their supplies of stamps from him upon requisition. These departments are charged for their total requisitions, then as the stamps are used and charged to the proper expense account or to customers' accounts, the departments are credited on the books of the bank.

### Certification of Instruments

Frequently checks or other instruments are presented at the windows of the bank for certification rather than for payment. In certifying an instrument the bank stamps upon the face of the instrument the word "certified," signifying that it agrees to honor the instrument when presented for payment. When a bank has thus certified an instrument it becomes itself the principal debtor, and the maker of the instrument has only a contingent liability at the most. A check of this sort becomes an obligation of the bank and its acceptability and its security are enhanced to the extent that the check is now dependent upon the solvency of the bank for its redeemability. It is no longer subject to imperfections due to stop-payment orders, insufficient funds, etc. Such an instrument is a satisfactory substitute for money. Accordingly certified checks are extensively used in making payments as evidence of good faith in connection with sealed bids, in paying taxes and making other payments to the government, and in making settlements of transactions between stock brokers, bond dealers, etc. Certified checks, however, are not legal tender.

In most banks the paying teller of the bank attends to the work of certification. Among the customers of the bank upon whose practices this study is based are many stock brokers. By a rule of the New York Stock Exchange these brokers are required to use certified checks in settling balances due each other from their trading operations. The bank likewise requires that stock brokers use certified checks in making their deposits. By this means funds are created which offset its own certifications. The work of certification in such a bank, therefore, becomes unusually heavy with the result that it is necessary to operate a specialized certification department in order that this work may be properly handled.

### **Routine of the Certification Department**

From the standpoint of the bank the act of certifying a check is similar to that of paying it. By the act of certification the bank practically waives the right to refuse to pay the check, hence it is necessary for the certification clerk to take the same precautions to examine items for signatures, filling, date, stop-orders, adequacy of balance, etc., as does the paying teller. A person desiring to have an item certified delivers that item at one of the windows of the certification department and receives a numbered identification ticket in exchange for it. He then waits until the process of certification is completed, or else if the window man anticipates delay in passing the item, the presenter returns for it later. The item then comes to the attention of the certification clerk for examination. Having satisfied himself that all is in order, he places the certification stamp, together with his signature, upon it.

The certification clerk has on file a list of the stop-payment orders which have been sent by the stock brokers, a record of the balance of these accounts at the beginning of the day's business, together with whatever day loans may have been added to them, and he makes it a part of his preparation for his work to familiarize himself with the signatures of these customers. Checks drawn by these regular customers are passed upon immediately. Regarding items drawn by other customers of the bank there is likely to be some doubt as to the advisability of certifying them. The certification clerk has "holds" or temporary debits placed against the accounts of the drawees of these items by communicating with the bookkeepers by means of the telautograph, and he may deem it necessary to send the checks to the signature department for examination of the signatures. Each item to be charged to the account of a foreign depositor is sent to the foreign bookkeeper's department where it is carefully examined and

a "hold" is placed against the account. In addition the sanction of an officer of the bank is required before it can be certified. After items have been passed upon in this manner they are entered on the proper posting sheets from which charges are made to the proper accounts, there being one sheet for each customers ledger. The checks are then stamped "certified" and delivered to the applicants.

### **Delivery of Certified Instruments**

The identification ticket which was given to the applicant or his messenger in exchange for the instrument to be certified serves an important function in that it expedites the work of certification and affords some assurance that the certified item will fall into the hands of the rightful owner or a party authorized to receive it. Each of these tickets is given a serial number and the same number is stamped upon the instrument which is to be certified. To obtain the certified instrument the applicant is required to surrender the corresponding identification ticket upon which appears the name of his firm together with his own signature. The bank then files these identification tickets as evidence that delivery has been made.

### **Miscellaneous Items Certified**

In addition to certifying checks, the bank receives each morning from certain of its correspondents letters asking it to protect their notes at maturity. These letters are examined by the bookkeepers for sufficient funds, the balance of the account is noted on the letters, and they are initialed and sent to the certification department for reference. In addition to this rather special class of instruments, such others as notes, drafts, trade acceptances, etc., when made payable at a bank, are suitable material for certification. Aside from calling upon the foreign bookkeepers to make a careful investigation of whatever foreign items may be sent in for certification, the

certification clerk handles these other instruments just as he does checks

### **Recording Certified Instruments**

The accounting work in connection with certified checks consists in debiting the accounts of the customers who drew the checks and crediting the account "Certified Checks Outstanding" at the time of certification. When the check returns to the bank and is paid, Certified Checks Outstanding is debited. The balance of this account therefore constitutes the liability of the bank for certified checks.

Specifically this accounting work is carried out in the following manner. At the close of the day's business the posting sheets of the certification clerk are sent to the customers bookkeepers who charge the items to the accounts of those who drew them. Then the sheets are turned over to the certified check bookkeeper who is attached to the customers bookkeepers and who keeps the Certified Checks Outstanding account. Instead of crediting the items on the same day he holds up the entries until the day following certification. On that day most of the certified checks return to the bank and are simply marked off the certification sheets. The open items are then credited to the Certified Check account. Later on as these outstanding checks come in for payment they are debited to this account. The outstanding certified check book thus constitutes a record of the liability of the bank for certified checks.

### **Follow-Up of Outstanding Certified Items**

At intervals the outstanding certified check book is compared with the records of the general bookkeeping department, which records are compiled from reports sent in by the certification clerk and by the check desk, and its accuracy is ascertained. The outstanding certified checks continue as

liabilities of the bank until paid by it. It is the policy of the bank to follow up these outstanding items at intervals, say monthly, and to attempt to have them presented for payment by the holders.

In case an item of this sort has been mislaid, stolen, lost, or destroyed, and the maker desires credit for it, the certifying bank requires him to file an indemnity bond for double the amount of the check, relieving the bank of responsibility in the matter. If a depositor has a check certified, which later for some business or personal reason he finds he cannot use, the problem of canceling the check arises. The most satisfactory way of retiring such an instrument is for him to deposit it in his own account. The check thus reaches the check desk through the regular channels where it is stricken off the outstanding certified check book and is again credited to his account. Regardless of whether a check of this sort is payable to bearer or to some specified payee it is sufficient that only the maker indorse it for the purpose of redepositing it.

## CHAPTER IV

### CLEARING

#### Nature of Clearing Operations

The clearing house is an agency both for collecting cash items and for paying them. The clearing process consists in exchanging the items which a bank holds drawn on other member banks for the items which they hold drawn on it. The paying and collecting operations are thus made reciprocal, the amount collected is used to offset the amount paid and only the balance is settled in cash or other funds.

For the purpose of carrying on the clearing operations, banks associate themselves into clearing house associations, or "clearing houses," as such associations are termed. While in discussing the work of clearing it is necessary to consider the activities of an institution outside the bank, it must be borne in mind that the clearing house is related to the several banks which use its facilities in much the same way as one of their departments. In fact, the clearing house may be considered as a joint collection and check-paying department of the banks making up its membership.

#### The New York Clearing House Association

Clearing house associations, numbering at the present time some two hundred or more, are to be found in all large cities of the United States. Of these associations, that of New York, which was founded in 1853, is both the oldest and in every sense of the word the largest. The above-named clearing house association consists of some sixty banks located in Greater New York, including the New York Federal

Reserve Bank<sup>1</sup> The organization is an unincorporated, co-operative association deriving its authority over members through their having given written assent to its constitution

The constitution of the New York Clearing House provides for the regulations of the association and the guidance of its members Administration of the affairs of the association is vested in certain officers and standing committees chosen by vote of the members in annual meetings. Of the officers, the president and secretary exercise the powers which are usually vested in officers of the same designation in other types of organizations The manager of the association is an important official He is appointed by the clearing house

<sup>1</sup> The members as of October 1, 1920, together with their clearing house numbers, are as follows

1 Bank of New York, N B A	78 Commonwealth Bank
2 Bank of the Manhattan Company	81 Garfield National Bank
4 Mechanics' and Metals National Bank	82 Fifth National Bank
6 Bank of America	85 Seaboard National Bank
8 The National City Bank of New York	91 Liberty National Bank
12 Chemical National Bank	96 State Bank
13 Atlantic National Bank	99 Coal and Iron National Bank
15 National Butchers' and Drovers' Bank	100 Union Exchange National Bank
17 Greenwich Bank	102 Brooklyn Trust Company, Brooklyn
21 American Exchange National Bank	103 Bankers' Trust Company
23 National Bank of Commerce	104 U S Mortgage and Trust Company
28 Pacific Bank	106 Title Guarantee and Trust Company
30 Chatham and Phoenix National Bank	107 Guaranty Trust Company
33 Hanover National Bank	108 Fidelity International Trust Company
44 Metropolitan Bank	110 Lawyers' Title and Trust Company
45 Corn Exchange Bank	111 Columbia Trust Company
53 Importers' and Traders' National Bank	113 Peoples' Trust Company, Brooklyn
54 National Park Bank	114 New York Trust Company
59 East River National Bank	116 Lincoln Trust Company
63 Second National Bank	117 Metropolitan Trust Company
65 First National Bank	118 Nassau National Bank, Brooklyn
67 Irving National Bank	120 Federal Reserve Bank of New York
70 Bowery Bank	121 Farmers' Loan and Trust Company
71 New York County National Bank	122 Columbia Bank
72 Continental Bank	123 Equitable Trust Company
74 Chase National Bank	200 New York Clearing House (City Col-
76 Fifth Avenue Bank	lection Department)
77 Commercial Exchange Bank	

It will be noted that certain numbers are omitted This is due to the fact that as the numbers are vacated the vacancies are not filled New members take the next highest number The city collection department of the Clearing House is given the distinctive number 200 in keeping with its special relations to the members of the association

The Federal Reserve Bank of New York has the status of a special member As such it was not required to sign the constitution and it has no vote It is not required to furnish a weekly statement nor is it subject to the rules regarding collection charges In other respects it has the status of a regular member of the association



committee, but by custom the same manager is retained from year to year, in fact there have been only four incumbents of this office in the sixty-five years of the existence of the association. The manager has full charge of the clearing operations. He controls the clerks and employees of the association as well as the employees of member banks during the work of clearing. As superintendent of the clearing house session he is responsible for maintaining discipline on the exchange floor, adjusting balances, imposing fines for violation of the rules of procedure, keeping records of the operations of the association, etc.

### Clearing House Committees

There are five standing committees as follows: clearing house, conference, admission, nominating, and arbitration. With the exception of the clearing house committee the work of these committees is comparatively light. The clearing house committee, however, is an exceptionally powerful and active body, being next to the association itself in authority. It provides for the maintenance of the association and it may draw upon members for their quotas of the expense. The salaries of all employees save those of the manager and the assistant manager are fixed by this committee. It may examine a member bank and, if it deems such a course necessary, it may require the bank to deposit securities to protect its balances which result from the clearings. Subject to the approval of the association the clearing house committee is empowered to fix fines for errors and to establish rules governing proceedings when they are not provided for in the constitution.

It may also legislate upon the subject of collections outside New York City. Finally, all applications of banks for membership or for the privilege of clearing through members come to this committee, the latter for final action, the former for

approval before they can be considered by the committee on admissions. When their conduct merits it members may be temporarily suspended by the clearing house committee acting in conjunction with the conference committee.

### **Admission of Members**

New members may be admitted to the association by the approval of their applications by both the clearing house committee and the committee on admissions, and by a favorable vote of three-fourths of the members of the association who are present at the meeting at which the application is considered. A requirement that applicants shall have an unimpaired minimum combined capital and surplus of \$1,000,000 is in effect. The new member is required to signify its assent to the constitution in writing and to pay an admission fee which varies with its capital and surplus. Banks having a capital and surplus of over \$5,000,000 pay an admission fee of \$7,500, those having a capital and surplus of \$5,000,000 or less pay \$5,000.

A member may be suspended by the joint action of the clearing house and the conference committees. Expulsion of a member may be effected only by an affirmative vote of the majority of the members. A member may withdraw from the association whenever it wishes to do so, provided it pays its share of the expenses of the association up to the time of withdrawal.

### **Non-Members Clearing Through Members**

The volume of clearings of many banks is not sufficient to pay them to become members of the association. Provision has been made whereby such banks may arrange with other banks who are members to clear for them, but an arrangement of this sort must first have the sanction of the clearing house committee. Banks enjoying this privilege are required to pay

\$1,500 annually, to submit to examination by the clearing house examiner, and to furnish reports to the association in the same manner as members. Some fourteen banks make use of the facilities of the association in this way, in addition to over one hundred branches of clearing house members.

### **Expenses**

The expenses of the association, with the exception of those arising from the work of the department of examinations, are apportioned among members pro rata, according to the average amount which each member has sent to the clearing house during the preceding year. A minimum charge of \$1,000 per year, however, is made against each member. The expenses of the department of examination are assessed separately against each member on the basis of that member's gross assets.

### **Functions of New York Clearing House**

The objects of the New York Clearing House Association as set forth in its constitution are "the effecting at one place of the daily exchanges between the members thereof and the payment at the same place of the balance resulting from such exchanges, the promotion of the interest of the members, and the maintenance of conservative banking through wise and intelligent co-operation."

Concretely, these rather broad subjects have found expression in such activities as

- 1 Effecting exchanges of cash items
- 2 Collecting city and country items
- 3 Establishment of certain uniform practices among members for their mutual protection and benefit.
- 4 Mutual support in times of stress
- 5 Examination of members from time to time
- 6 Publication of reports on the condition of its members

The first of these functions is more properly the material to be considered in this chapter. A few words, however, should be said regarding the other functions of the association.

### **City and Country Collections**

Within the last few years the New York Clearing House has made collections of country items as well as city items for its members. The former were handled by a country collection department. This department had a successful career, but after the establishment of the federal reserve system and the extension of the collection service of the federal reserve banks the department was closed up. More recently a city collection department has been organized and is in successful operation. The function of this department is to make collection of certain city items for member banks.

### **Regulation of Interest on Deposits**

An important item of the New York Clearing House, to quote from the constitution of the association, is "the maintenance of conservative banking." The association's efforts in this direction have consisted in fixing maximum rates of interest to be allowed on depositors' balances and minimum charges to be made for collection and exchange services, and in establishing uniform requirements as to the amount and definition of cash reserve to be kept against deposit liability.

### **Interest Rates**

It is not sound and conservative banking to offer a rate of interest on depositors' balances which is in excess of the net profit remaining after the cost of providing service for that account has been deducted from the return which comes to the bank from loaning the balance. On the other hand, each bank is obliged to a great extent to meet whatever rates other banks of the same class offer to their depositors. Obvi-

ously the problem of interest rates on balances is one for co-operative rather than individual solution

The rule of the clearing house association concerning interest rates to be allowed by member banks and banks clearing through member banks recognizes three types of deposits

1. Deposits or certificates of deposit payable on demand or within 30 days, due to banks and bankers located in the United States or Canada, except a mutual savings bank located in the New York Federal Reserve District
2. Deposits or certificates of deposit due to any mutual savings bank located in the New York Federal Reserve District, to any concern other than a bank, or to an individual
3. Time deposits, consisting of all deposits payable after 30 days

The rule in all cases fixes the maximum rate which may be allowed on deposits. This amount differs with the different classes. In the case of demand deposits due to banks and bankers the rate is variable, being based upon the discount rate for 90-day commercial paper which obtains at the New York Federal Reserve Bank. When the 90-day discount rate is 2 per cent or less, clearing house banks are permitted to allow a maximum rate of 1 per cent per annum on such deposit balances. For each  $\frac{1}{2}$  per cent in excess of 2 per cent which the federal reserve rate shows, clearing house banks may increase their rates to depositors by  $\frac{1}{4}$  per cent, except that the rate to be allowed depositors shall not in any case exceed  $2\frac{1}{4}$  per cent per annum. The maximum rate of interest which can be allowed on deposits of mutual savings banks in the New York district, of individuals, etc., as well as the rate of interest on time deposits, does not fluctuate with the rediscount rate for 90-day commercial paper, but has been fixed

at 3 per cent on the former and  $3\frac{1}{2}$  per cent on the latter class of deposits.

The foregoing provisions do not apply to the account of, or to any certificate of deposit issued to, any customer residing in and transacting business in any foreign country other than the Dominion of Canada, or to any business association or corporation organized and located therein. Neither are the provisions to be construed as affecting such interest rates as are or may be fixed or regulated by law.

### **Exchange Charges**

Another tendency among keenly competing banks located in the leading collection centers is to charge an excessively low rate of exchange on country items, if possible, or to make no charge at all. To alleviate such a condition and place the collecting machinery of its members upon a self-supporting basis, the clearing house has made a rule to the effect that each of the banks which uses its facilities shall assess and collect exchange against depositors for certain transit items deposited by them.

### **Reserves**

Finally the clearing house association also works in the interest of maintaining conservative banking practices by regulating the amount and kind of reserve against deposit liability which clearing banks must keep. This rule states that each bank must maintain a reserve of the same proportions and definition as that required by the laws under which it operates. In computing the amount of net demand deposits upon which reserve is to be figured, however, banks are restrained from deducting deposits secured by the deposit of outstanding unmatured stocks, bonds, or other obligations of the state or city of New York, or deposits to the amount of the stocks, bonds, or other obligations of the state or city

of New York owned and held by the bank. The clearing house regulation further provides that all required reserve other than that which is in the form of cash on hand must be maintained in the form of a deposit with the New York Federal Reserve Bank, or in some other bank which is a member of both the federal reserve system and the clearing house association, or with any other member of the association which maintains in the Federal Reserve Bank of New York the reserve required by member banks

### **Mutual Support in Times of Stress**

The mutual support which the clearing house banks have given each other through their organization has consisted of the issuance of loan certificates to members in times of stress in exchange for the pledge of certain of the unmatured assets of these banks. One of the characteristics of financial stress is an abnormal demand for money. Before the establishment of the federal reserve banks, the banks of New York City could obtain money to satisfy the demand which accompanied financial disturbances only from their own vaults. As their cash in the vault became low, the problem of conserving the supply naturally became a pressing one. In those days clearing house balances were settled in cash until someone happily devised the scheme of substituting clearing house loan certificates for the cash which was used in this manner. Under this system a bank which was in need of funds took to the clearing house certain collateral consisting of bonds, commercial paper, etc. A committee appointed especially for the purpose passed upon this collateral, and if all was in order clearing house loan certificates were issued against it. The applicant bank was permitted to use these certificates in lieu of cash in paying its clearing house debit balances, and it could use a corresponding amount of cash in order to fill other needs.

## **Examinations and Reports**

The clearing house association also maintains an examination department. It is the business of the clearing house bank examiner to make an examination of and a report on the condition and practices of each clearing bank at least once a year. In addition, special examinations are made at the discretion of the clearing house committee, and also by constitutional requirement, when any clearing bank undergoes a change of management or when two or more are merged, consolidated, etc. Clearing house examinations are designed to supplement those which are made by public officials. The latter type of examination is mainly for the purpose of discovering and bringing to punishment actual violators of the law. While such examinations are usually effective in discovering and bringing to justice those who have broken the law, the public authorities are generally without the power to enforce the correction of minor irregularities and practices which if unchecked might finally wreck a bank or impair the faith of the public in the clearing house members. It is to supply this deficiency that the clearing house examination has been instituted.

## **Report of Condition of Member Bank**

In addition to submitting to examination, every bank which clears through the association, excepting the Federal Reserve Bank of New York, is required to furnish a weekly report of its average daily condition, also a statement of its actual condition at the close of business on each Friday. These reports contain a total of the loans, discounts and investments, reserves, deposits, and circulation of the bank.

## **Statement of Clearing House Banks**

The required reports give the association information regarding the standing of each member. Aside from serving



# STATEMENT OF THE MEMBERS OF THE NEW YORK CLEARING HOUSE ASSOCIATION

FROM REPORTS AS REQUIRED UNDER ARTICLE III OF THE CONSTITUTION  
For Week Ending Saturday, October 23, 1920.

No.	CLEARING HOUSE MEMBERS	*CAPITAL	*NET PROFITS	Loans, Disc'd Investments, etc.	CASH IN VAULT Average	Reserve with Legal Depositories Average	NET DEMAND DEPOSITS Average	TIME DEPOSITS Average	National Bank Circulation Average	Note
<b>MEMBERS OF FEDERAL RESERVE BANK</b>										
1	Bank of New York N. Y. & A.	\$2,000,000	\$7,167,000	\$45,468,000	\$ 797,000	\$ 4,676,000	\$12,517,000	\$3,680,000	\$771,000	1
2	Bank of the City of New York	5,000,000	16,199,100	125,970,000	2,932,000	12,005,000	12,585,000	13,535,000	1,000,000	2
3	Bank of the Manhattan Co.	10,000,000	16,512,800	913,993,000	10,112,000	10,000,000	12,881,000	4,125,000	1,000,000	3
4	Bank of America	5,500,000	6,044,300	60,241,000	10,000,000	7,895,000	17,439,000	1,548,000	1,200,000	4
5	Bank of Montreal	40,000,000	\$ 64,469,200	539,553,000	13,724,000	61,513,000	(a) 375,392,000	41,716,000	1,200,000	5
6	National City Bank									6
<b>NOT MEMBERS OF FEDERAL RESERVE BANK</b>										
151	Columbia Bank	3,000,000	1,524,100	32,353,000	728,000	3,112,000	32,370,000	114,000		151
152	Equitable Trust Co.	12,000,000	17,640,300	168,729,000	1,831,000	19,807,000	(c) 176,337,000	14,045,000		152
<b>NOT MEMBERS OF FEDERAL RESERVE BANK</b>										
17	Greenwich Bank	1,000,000	1,840,000	18,363,000	2,611,000	1,793,000	19,099,000	3,000		17
70	Bank of the State	250,000	844,100	5,781,000	718,000	2,341,000	5,679,000	40,869,000		70
96	State Bank	2,500,000	2,331,700	70,248,000	3,483,000	2,072,000	30,294,000			96
<b>TRUST COMPANIES</b>										
<b>NOT MEMBERS OF FEDERAL RESERVE BANK</b>										
106	Title Guaranty & Trust Co.	6,000,000	19,281,900	48,882,000	1,056,000	3,710,000	31,509,000	1,105,000		106
110	Lawyers Title & Trust Co.	4,000,000	6,359,300	37,312,000	961,000	1,446,000	16,080,000	334,000		110
<b>TOTALS: Federal Reserve Bank</b>										
5	Members of Federal Reserve Bank	362,000,000	460,418,100	\$ 374,793,000	95,198,000	547,493,000	\$ 4,084,793,000	24,632,000	34,673,000	
17	Not members of Federal Reserve Bank	2,750,000	5,035,800	94,872,000	4,196,000	4,196,000	55,073,000	40,873,000		
96	Trust Companies, not members of Federal Reserve Bank	10,000,000	18,602,100	70,194,000	2,037,000	5,195,000	47,159,000	1,430,000		
<b>Aggregates 53 Members</b>										
		\$76,650,000	\$84,081,400	\$445,859,000	104,046,000	\$56,798,000	\$ 4,137,454,000	269,121,000	34,673,000	
<b>COMPARISONS</b>										
				Decrease	Decrease	Decrease	Decrease	Increase	Increase	
				40,275,400	632,000	7,091,000	14,421,000	6,455,000	126,000	

\*As per official reports

12 National, Sept. 3, 1920

13 State, Sept. 24, 1920

14 City, Sept. 24, 1920

15 of Oct. 2, 1920

Includes Deposits in Foreign Branches \$1,300,424,000 not included in total liability:		Balance earned in bank in foreign countries as interest on such deposits.	
(a)	3,510,000	"	\$47,945,000
(b)	104,785,000	"	243,000
(c)	19,223,000	"	2,675,000
(d)	23,142,000	"	7,715,000
(e)		"	7,715,000

Bills Payable, Rediscounts, Acceptances and other Liabilities \$1,777,657,000		Reserve required on Net Demand Deposits.	
		Time	
		\$51,023,000	
		7,401,300	
Members Federal Reserve Bank		Based on Time Deposits	
State Banks not members of Federal Reserve Bank		Deposits.	
Trust Companies not members of Federal Reserve Bank		Excess	
Totals		Total Net	
		\$515,478,700 Excess, \$10,128,300 Decrease	
		\$5,731,100	

## ACTUAL CONDITION THIS DAY

TOTALS		Reserve required on Net Demand Deposits	
		Time	
		\$514,849,460	
		7,477,500	
Members Federal Reserve Bank		Based on Time Deposits	
State Banks not members of Federal Reserve Bank		Deposits.	
Trust Companies not members of Federal Reserve Bank		Excess	
Totals		Total Net	
		\$515,478,700 Excess, \$10,128,300 Decrease	
		\$5,731,100	

Bills Payable, Rediscounts, Acceptances and other Liabilities \$1,779,710,000		Reserve required on Net Demand Deposits	
		Time	
		\$514,849,460	
		7,477,500	
Members Federal Reserve Bank		Based on Time Deposits	
State Banks not members of Federal Reserve Bank		Deposits.	
Trust Companies not members of Federal Reserve Bank		Excess	
Totals		Total Net	
		\$515,478,700 Excess, \$10,128,300 Decrease	
		\$5,731,100	

Clearance for Week ending October 23, 1930,		October 23, 1930	
		\$4,523,279,313	
Clearance this Day		October 16, 1930	
		\$4,506,464,539	
x 5 Days		October 23, 1930	
		\$4,477,633,165	

Clearance for Week ending October 23, 1930, \$4,523,279,313  
 x 5 Days, \$4,506,464,539  
 October 23, 1930, \$4,477,633,165

Clearance for Week ending October 23, 1930, \$4,523,279,313  
 x 5 Days, \$4,506,464,539  
 October 23, 1930, \$4,477,633,165

Clearance for Week ending October 23, 1930, \$4,523,279,313  
 x 5 Days, \$4,506,464,539  
 October 23, 1930, \$4,477,633,165

admirably their purpose of acting as a check upon the condition and practices of each clearing bank, these reports are combined into a weekly statement of clearing house banks (Form 8) and published by the association. If properly understood and interpreted, these reports furnish a very serviceable barometer of business condition throughout the United States.

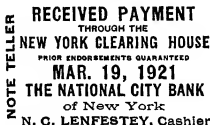
### **The Process of Clearing**

Effecting exchange of items drawn upon its members is the essential function of a clearing house association. The operation, as already explained, is simply one of collecting those checks, drafts, etc., contained in the daily receipts which are drawn on clearing house members, and of paying the items which the member banks in turn hold against the bank.

The items which may be sent by a bank through the clearing house include in general all cash items payable by the banks which are entitled to use the facilities of the association. Thus all certified items, ordinary checks, clean drafts and bills of exchange, notes and acceptances which are due and which are drawn upon or payable at clearing house banks, are regularly sent through the exchanges. The rules of the association, however, exclude items drawn by a concern transacting business in New York upon non-clearing banks but made payable if desired by a clearing bank. Such items can be cleared only if they are accepted and made payable through the New York Clearing House by the bank upon which they are drawn. Furthermore, such checks, when drawn on a non-clearing bank but made payable at a clearing non-member bank, cannot under any condition pass through the exchanges. Items which bear restrictive or qualified indorsements, such as "For Collection," "For Account of," etc., are also excluded unless the sending bank guarantees all indorsements which precede its own.

### Indorsement of Items for Clearing

In practice it is virtually impossible for a sending bank to examine the indorsement on every one of the thousands of checks which it daily sends through the exchanges, hence it is the custom to guarantee previous indorsements on all clearing house items. The association requires that all items which are to be cleared bear indorsement acknowledging receipt of payment through the clearing house. The bank accordingly uses upon each clearing house item a uniform indorsement stamp which conforms to both of these provisions. As the



Form 9 Indorsement on Clearing House Check (Size 2 x 1  $\frac{3}{4}$ )

first step in the process of preparing the items for clearing each item is run through an indorsing machine which places upon it the stamp shown above (Form 9).

### Work of the Assembly Racks

Inside the bank the process of preparing items for clearing is practically a continuous one. Beginning just after ten o'clock in the morning, when the day's regular clearing sessions are over, the clearing house items of the various departments of the bank are sorted into five divisions as a regular part of the process of proving the receipts of those departments. These divisions, which correspond to the division of labor in the assembly rack department, are as follows:

A	containing	items	drawn	upon	clearing	house	banks	numbered	1- 23
B	"	"	"	"	"	"	"	"	28- 54
C	"	"	"	"	"	"	"	"	59- 76
D	"	"	"	"	"	"	"	"	77-100
E	"	"	"	"	"	"	"	"	102-122

In the late afternoon, after the work of the various operating departments has been proved, the clearing house items are passed to the assembly rack department the function of which is to complete the process of preparing them for the clearing house session held the following morning. A special force of the assembly rack department handles the material in each of the five divisions into which the clearing house items were separated by the operating departments.

Each of the units of the assembly rack department sorts its items according to drawee banks. During the process batch proofs are prepared which show that the total amount distributed to the banks equals the amount received by the unit. After the work of sorting has been completed the items to be presented for payment to each bank are listed and enclosed in a standard form envelope to the outside of which the list of contents is attached.

Proof of each section of the work is obtained by combining the batch proofs. The section proofs are further combined to form the departmental proof. This proof shows that the amount charged to the department equals the amount enclosed for the various drawee banks by the units.

### Mail Teller's Work

While the bank's clearing house receipts of the previous day are being prepared for clearing by the assembly rack department, the mail teller's night force is busily engaged in sorting and proving the night mail receipts. By early morning a considerable mass of clearing house checks has accumulated. Many more such items are contained in the morning mail. The various tellers and departments of the bank also receive

at times in their early morning work large clearing house items which should be passed through the clearing house that day. In order to prepare such items received for the morning clearings and thereby save a day's interest on them a special assembly rack is operated in connection with the mail teller's department. Such mail and early morning departmental clearing house items are added to the exchanges for the day as prepared by the assembly rack department. When all possible exchanges have passed through the racks, an assembly rack proof (Form 10) showing the combined results of the day's work is prepared.

### Forms Required at Clearing House

After the assembly rack work has been completed the mail teller's assembly rack force prepares the forms which are required at the clearing house session. These forms are as follows:

- 1 The exchange slip. This is a list of the items to be delivered to a given bank. One is made up for each bank against which claims are presented and the slip is then attached to the outside of the envelope containing the claims, or "exchanges," as they are called.

2. The "small ticket." One of these is made out and presented to each bank of the clearing house. This ticket shows the name of the bank against which the claims are presented, the name of the claimant, and the aggregate claim brought.

- 3 The "first ticket" (Form 11). This is for the use of the proof clerk of the clearing house and consists of a ticket showing the date, name, and clearing house number of the claimant bank and the aggregate claims or exchanges brought by it for the day.

- 4 The settling clerk's receipt form. This form is for the purpose of securing the receipt of the banks against which

EXCHANGES FOR THE CLEARING HOUSE									
RACK # 5		DATE March 21 1921							
No.	AMOUNT	No.	AMOUNT	No.	AMOUNT	No.	AMOUNT	No.	AMOUNT
1	512 629 65	26	2 121 150 85	50	97 336 50	77	464 310 55	102	270 644 09
2	520 426 51	27	686 916 06	51	26 118 106	78	272 981 30	103	62 216 46
3	1 600 023 35	28	1 865 205 91	52	276 394 106	79	264 006 59	104	113 735 15
4	343 109 86	29	442 593 156	53	43 342 72	80	106 250 36	105	174 551 87
5	1 006 169 63	30	266 265 922	54	291 975 54	81	62 724 03	106	77 765 17
6	267 205 95	31	641 737 39	55	436 755 08	82	36 660 77	107	27 494 14
7	202 422 26	32	156 309 55	56	113 840 87	83	142 850 69	108	114 024 16
8	144 323 95	33	356 445 99	57	115 840 87	84	33 953 69	109	36 200 92
9	700 715 95	34		58	424 737 23	85	80 517 55	110	64 210 13
10	145 810 86			59	175 490 56	86	315 190 64	111	233 410 79
11	732 327 51	70		60	85 860 94	87	298 632 77	112	225 420 94
12						88		113	423 521 40
13						89		114	19 625 97
14						90		115	16 015 46
15						91		116	59 835 70
16						92		117	1 104 464 44
17						93		118	76 746 53
18						94		119	67 077 57
19						95		120	155 331 95
20						96		121	
21						97		122	
22						98		123	
23						99		124	
						100		125	
								126	
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								P O	

Form 10 Assembly Rack Proof. (Size 17 x 8 3/4)

claims are presented. It consists of the names of the clearing house banks arranged in order of their clearing house numbers on the left side, followed to the right by columns for the total claim against each and the signatures of their clerks who receive the claims. All but the columns for signatures is completed at this time

New York Clearing House.	No 8.	New York Clearing House,
		<u>May 3</u> 1921
	Credit THE NATIONAL CITY BANK, \$	<u>14,842,144.32</u>
		<u>G. L. Davidson</u> Selling Clerk

Form 11 Clearing House First Ticket (Size  $8\frac{1}{2} \times 3\frac{1}{2}$ )

### Clearing Operations

The exchanges are now ready to be taken to the clearing house to be presented to the drawee banks. There are two regular sessions at the New York Clearing House, one at nine o'clock and the other at ten o'clock. At nine o'clock most of the member banks meet together and merely exchange whatever items they have been able to prepare for clearing at that time. Since most of the large banks operate night forces, or assembly racks, a large part of the day's exchanges are transferred at this time. No forms are exchanged and no settlement is made until the ten o'clock session. The early session is purely an expedient to give the banks a start of one hour upon the incoming checks. The check clerks and the bookkeepers of each bank are thus enabled to begin the work shortly after nine o'clock, instead of being obliged to wait until after ten.

The main session of the clearing house occurs at ten o'clock.



Shortly before that hour a representative of the receiving teller's department takes charge of the items prepared by the morning assembly racks, together with the forms showing the totals of exchanges made at both clearing sessions. The representative of the receiving teller's department, who is to be known as the bank's settling clerk at the clearing house session, has charge of the force of the bank which is required to effect the exchanges.

### **Force for Effecting Clearing**

The bank's force for clearing may consist at times of as many as eight men, comprising whatever messengers, porters, and clerks the volume of the work may require. The essential operations of clearing, however, may be reduced to two—that of making delivery of items to drawee banks, and that of receiving and recording items presented against the bank and completing the records required by the bank and the clearing house association. Reduced thus to its simplest terms the clearing house operation on the part of a given bank may be performed by two clerks, a delivery clerk and a settling clerk, to whom respectively are delegated the tasks mentioned above. For the sake of simplicity it will be assumed in the discussion to follow that the work of clearing is handled by two clerks.

### **Making Exchanges**

Inside the clearing house everything is for order and precision. Upon the exchange floor, desks are arranged in rows and each bank is assigned a desk according to its clearing house number. The settling clerk stations himself behind the desk assigned to his bank while the delivery clerk, with his envelopes, exchange slips, and small tickets, together with the form for obtaining the receipts of each bank to which he makes delivery, stations himself in front of the desk.

Promptly at ten o'clock the signal for starting the exchange of items is given by the clearing house manager or his assistant. Each delivery clerk moves forward past the desk of each of the other banks until he has visited them all and returned again to the desk of his own bank. As he passes each desk he leaves with the settling clerk stationed there the envelopes containing the items, the exchange slips, and the small ticket for that particular bank. Presenting his settling clerk's receipt form to the settling clerk before him, he obtains as a receipt that clerk's initials opposite the listed amount.

When all of the delivery clerks have completed their circuits an exchange has truly been made. Each bank has presented for credit those items which it held for other members of the clearing house association, and in return it has had presented to it every one of its own checks which other members of the clearing house wished to have it honor.

### **Settling Clerk's Statement**

After the exchanges have been received the settling clerk prepares his statement (Form 12). The credit column of this statement sheet represents claims which have been brought to the clearing house by the settling clerk's bank. An entry of these amounts was made at the time the assembly rack proof was completed. The settling clerk completes the statement by entering from the exchange slips, attached to the envelope containing the exchanges, the amounts which have been presented against his bank. The columns are then footed, the footings proved against the totals of the small tickets received, and the amount and character of the balance determined.

The items which the bank has received at the clearing house are of no further service in the work of clearing. They are accordingly taken to the bank by the delivery clerk where they are received by the check desk to be examined, proved, and debited to the proper accounts of the bank.

No 8 THE NATIONAL CITY BANK OF NEW YORK.					
Settling Clerk's Statement			May 3,		1921
No	BANKS	TOTAL DEBIT	No	BANKS	CR.
1	Bank of N Y Natl Bkg Assn	2,529,506 30	1	2,256,505 08	
2	Bank of the Manhattan Company	4,030,444 96	2	4,295,032 20	
3	Mechanics National Bank	391,181 87	3	757,841 11	
4	Mechanics & Metals Natl Bank	5,412,681 99	4	4,809,970 65	
6	Bank of America,	3,384,961 87	6	2,316,576 22	
12	Chemical National Bank	827,113 80	12	976,086 88	
59	East River National Bank	34,815 82	59	45,871 23	
63	Second National Bank,	398,768 45	63	118,791 87	
65	First National Bank	4,245,688 71	65	2,709,754 51	
67	Irving National Bank	1,098,224 70	67	1,387,422 73	
70	Bowery Bank,	9,559 63	70	7,947 14	
71	N Y County National Bank,	50,639 44	71	24,030 05	
72	Continental Bank,	650,001 33	72	814,519 48	
74	Chase National Bank,	5,104,457 52	74	5,654,482 58	
75	Assn Treas U S at N Y,	91,036 37	75	145,306 94	
76	Fifth Avenue Bank	510,941 93	76	50,892 16	
		12,194,133 90			
77	Commercial Exchange Bank	14,386 11	77	11,694 78	
78	Commonwealth Bank	11,514 23	78	5,400 02	
80	Lincoln National Bank	66,859 76	80	164,909 02	
81	Garfield National Bank,	46,625 29	81	45,674 92	
82	Fifth National Bank	20,979 38	82	38,557 33	
85	Seaboard National Bank	1,300,758 19	85	1,609,718 41	
91	Liberty National Bank	1,851,865 20	91	1,077,030 05	
92	N Y Produce Exchange Bank	144,111 27	92	87,870 49	
96	The State Bank	113,882 57	96	39,377 83	
99	Coal & Iron Natl Bank	223,015 12	99	126,623 90	
100	Union Exchange Natl Bank,	41,703 06		87,090 37	
		3,835,760 18			
		28,203,756 00		72,637,398 10	
		17,551,180 10		61,942,204,746 22	
		3,835,760 18			
		12,194,133 90			
		13,057,314 14			
		74,842,144 32		74,842,144 32	

After completing his statement the settling clerk makes his "second ticket" (Form 13). This consists of a small ticket for the use of the clearing house, showing the bank's debit for the amount of exchanges presented against it, its credit for the amount brought, and the amount and character of its balance. A copy of this second ticket is returned to the paying teller of his bank by the settling clerk to be used

New York Clearing House.	No 8	New York Clearing House,
		<u>May 3</u> 1921
	Debit National City Bank, Am't received, \$	<u>72,637,398.10</u>
	Credit " " " brought, \$	<u>74,842,144.32</u>
	\$ _____ Debit Balance Due Clearing House	
	Cr bal due NATIONAL CITY BANK, \$	<u>2,204,746.22</u>
		<u>C. L. Danulson</u> Settling Clerk

Form 13. Clearing House Second Ticket (Size  $8\frac{1}{2} \times 3\frac{1}{2}$ )

by the teller in preparing the clearing house section of his proof

### Clearing House Proof

Meanwhile the proof clerk of the clearing house prepares a proof of the day's work. When the settling clerks of the various banks appear at the clearing house they immediately send their first tickets to the proof clerk. From these tickets the latter prepares the third, or bank's credit, column of his proof sheet. As soon as the settling clerks complete them the second tickets arrive. From these the proof clerk prepares the other columns of his proof which are first, debit balance; second, bank's debit, fourth, credit balance.

The proof is completed when the total of the first column equals that of the fourth, and that of the second equals that of the third. In case a difference exists the amount is an-

nounced and the clerks set to looking for it. When the proof is completed the manager reads the balances in thousands of dollars. These balances are kept by the settling clerks to serve as a general statement of the day's clearings for the use of the officers of their respective banks.

### Settlement of Balances

The completion of the proof marks the close of the day's session at the clearing house. It is then in order to settle the various balances which have arisen from the day's transactions. Formerly these balances were settled by having the debtor banks bring to the clearing house actual cash or prescribed equivalents in settlement of their indebtedness. At a later hour the creditor banks appeared and received in cash the amount due them. Involving as it did the expense and risk of carrying millions of dollars in cash through the streets of the city each day, this system was both cumbersome and wasteful.

Since the organization of the federal reserve system this settling of balances has been attended to by the Federal Reserve Bank of New York. Under this system each member bank of the New York Clearing House Association which is not a member of the federal reserve system is required by the clearing house to keep a balance on deposit with the local federal reserve bank, or to make other arrangements for federal reserve funds with which to settle its balances. Since member banks of the federal reserve system are required by law to keep balances with the New York Federal Reserve Bank, this arrangement means that the Federal Reserve Bank of New York holds balances available for the use of each clearing house member in settling balances. At the close of the ten o'clock clearing the clearing house manager sends to the federal reserve bank a certified list of the day's balances. By a special agreement between the clearing house association, the member

banks, and the Federal Reserve Bank of New York, a book entry is made whereby the federal reserve bank debits the accounts of all clearing house debtors and credits the accounts of all of the creditor banks for the amount of their respective balances. Thus each creditor bank receives settlement for its balances in the form of an additional deposit to its credit with the local federal reserve bank. Likewise each debtor bank effects settlement by having a deduction made from its balance with the same bank.

The individual bank, when it has a credit balance at the clearing house, debits its account with the federal reserve bank entitled "Lawful Reserve with the Federal Reserve Bank," and when it has a debit balance it credits this account. Deposits with the federal reserve bank are the equivalent of cash, or better, since in the first place they can be converted into cash on demand, and in the second place they can be counted as legal reserve against deposits for which purpose cash itself cannot be used. The most desired medium of exchange has thus changed hands in the settlement of the clearing house balance with the least conceivable effort and at absolutely no risk from loss or theft.

### **Adjustment of Errors**

To return now to a consideration of the exchanges as they come from the clearing house, it must be borne in mind that they have the same status as other checks upon the bank itself which are presented for payment. As such they must be carefully examined for irregularities, signatures, insufficient funds, stop-payment orders, etc. In addition the receiving bank is obliged to determine whether the items for which it has already settled are really drawn upon it, and whether they have been properly listed and charged to it.

The rules of the clearing house association prescribe the procedure which members are to follow in adjusting errors

and in making returns which result from the day's clearings. All errors are to be adjusted between the banks themselves as the clearing house association assumes no responsibility for them. Items which are to be returned because they are not good or because they have been missent must be returned to the receiving bank the same day. The clearing house association provides certain fines which are assessed and collected from the offending banks by the one which has been injured through errors in delivering exchanges, missents, incorrectly listed items, etc. The work of searching out these items and presenting them for redemption and adjustment by the sending banks must be performed with accuracy and speed if the receiving bank is to avoid loss from failure to obey the clearing house regulations. The check desk of the bank accordingly begins work upon the incoming exchanges as soon as they are received. As soon as items which should be turned back to the clearing house banks are detected, they are sent to the city collection department for attention. For the convenience of members the association holds a special daily session at three o'clock in the afternoon in order that members may return items contained in the morning exchanges which they refuse to pay. At this session the city collection department returns all such items excepting those on which it is entitled to collect a fine from the offending bank. These are returned by messenger, the bank receiving in exchange for them a special redemption check which it puts through the clearings on the following day.

### **Summary of Clearing Operations**

The operation of clearing each day results in the collection of all the cash items drawn upon other member banks of the clearing house, which the bank holds, and in the paying of all similar items drawn upon itself which these other banks have accumulated. The impressive consideration in connec-

tion with the clearing house system of effecting collections and settlements is not so much the results which are accomplished, important as they may be, but rather the ease and efficiency with which those results are effected

The first consideration is economy in the use of money. During the years 1854 to 1919 inclusive the member banks of the New York Clearing House Association collected and paid \$3,317,819,113.123.32 in items through the clearing house by the transfer of only \$182,052,943.032 11 In other words, on the average only 5 48/100 per cent of the claims settled had to be paid by the actual transfer of funds This statement, however, does not bring out the whole truth During recent years a system of settling in cash has been supplanted by making settlements through the use of clearing house certificates, representing gold deposited by members with the clearing house association These certificates were non-negotiable except for the purpose of settling clearing balances More recently this system gave way to the one in use at the present time whereby balances are settled by transfer entries on the books of the New York Federal Reserve Bank.

The second consideration is that of economy of effort The only alternative to the scheme of collecting and paying items by the process of clearing is that of collecting by messenger As between a system of collecting all cash items drawn upon sixty banks and receiving all like items presented by them through the agency of a messenger and clerical force of not more than ten men who are employed at this work for about two hours each day on the average, and a system of sending messengers separately to present items to each of sixty banks and of accommodating in turn the messengers from those sixty banks who present and collect their items, there can be no comparison Furthermore the advantages which accrue to a given bank from having the items for col-



lection go out, and those for payment come in, at a regular and convenient time are considerable. Taking all into consideration—economies in the use of money and economies in effort—the clearing house is undoubtedly the most efficient banking machine in operation. The extent and growth of its operations are summarized on the table reproduced in Form 14 showing for each year, 1854-1919 inclusive, the total clearings for the year, total balances for the year, and percentage of balances and clearings.

TABLE SHOWING TOTALS OF CLEARINGS, BALANCES, AND THE PERCENTAGE OF BALANCES TO CLEARINGS

In the New York Clearing House for the Years 1854-1919 Inclusive

Fiscal Years Ending Sept 30	No of Clearing Members	Clearings for Year	Balances for Year	Balances to Clearings
1854	50	\$5,750,455,987 06	\$297,411,493 69	5 17%
1855	48	5,302,912,098 38	289,694,137 14	5 40
1856	50	6,906,213,328 47	334,714,489 33	4 83
1857	50	8,333,226,718 06	305,313,001 69	4 39
1858	46	4,756,664,386 09	314,238,910 60	6 66
1859	47	6,448,005,956 01	363,984,682 56	5 64
1860	50	7,231,143,056 69	380,693,438 37	5 26
1861	50	5,915,742,758 05	353,383,944 41	5 97
1862	50	6,871,443,591 20	415,530,331 46	6 04
1863	50	14,867,597,848 60	677,626,482 61	4 55
1864	49	24,097,196,655 92	885,719,204 93	3 67
1865	55	20,032,384,341 89	1,035,765,107 68	3 97
1866	58	28,717,146,914 09	1,066,135,106 35	3 71
1867	58	28,675,159,472 20	1,144,963,451 15	3 99
1868	59	28,484,288,636 92	1,125,455,236 68	3 95
1869	59	37,407,028,986 55	1,120,318,307 87	2 99
1870	61	27,804,539,405 75	1,036,484,821 79	3 72
1871	62	29,300,986,682 21	1,209,721,029 47	4 12
1872	61	33,844,369,568 39	1,428,582,707 53	4 22
1873	59	35,461,052,825 70	1,474,508,024 95	4 15
1874	59	22,855,927,636 26	1,280,753,176 12	5 62
1875	59	25,061,237,902 09	1,408,608,776 68	5 62
1876	59	21,597,274,247 04	1,295,042,028 82	5 99
1877	58	23,289,243,701 09	1,373,996,301 68	5 89
1878	57	22,508,438,441 75	1,307,843,857 24	5 81
1879	59	25,178,770,690 50	1,400,111,062 86	5 56
1880	59	37,182,128,621 09	1,516,538,671 29	4 07
1881	61	48,565,818,212 31	1,776,018,161 58	3 66

Form 14

1882	62	46,552,846,161	34	1,595,000,245	27	3 42
1883	64	40,293,165,257	65	1,568,983,196	15	3 89
1884	62	34,092,037,337	78	1,524,930,993	93	4 47
1885	64	25,250,791,439	90	1,295,355,251	89	5 12
1886	64	33,374,682,216	48	1,519,565,385	22	4 55
1887	65	34,872,848,785	90	1,509,626,324	77	4 49
1888	64	30,863,686,609	21	1,570,198,527	78	5 08
1889	64	34,796,465,528	87	1,757,637,473	47	5 05
1890	65	37,660,686,571	76	1,753,040,145	23	4 65
1891	64	34,053,698,770	04	1,584,635,499	88	4 65
1892	65	30,279,905,235	59	1,861,500,574	56	5 13
1893	65	34,421,380,869	50	1,696,207,175	52	4 92
1894	66	24,230,145,367	70	1,585,241,633	52	6 54
1895	67	28,264,379,126	23	1,896,574,349	11	6 71
1896	66	29,350,894,883	87	1,843,289,238	66	6 28
1897	66	31,337,760,947	98	1,908,901,897	67	6 01
1898	65	39,853,413,947	74	2,338,529,016	43	5 87
1899	64	57,368,230,771	33	3,085,971,370	53	5 37
1900	64	51,664,588,564	31	2,730,441,810	27	5 25
1901	62	77,020,672,493	65	3,515,037,741	05	4 56
1902	60	74,753,189,435	86	3,377,504,072	11	4 51
1903	57	70,833,655,940	29	3,315,510,487	48	4 68
1904	54	59,672,796,804	41	3,105,858,575	60	5 20
1905	54	91,879,318,369	00	3,953,875,974	80	4 33
1906	55	103,754,100,091	25	3,832,621,023	87	3 69
1907	54	95,315,421,237	96	3,813,926,108	35	4 00
1908	50	73,630,971,913	18	3,409,632,271	41	4 63
1909	51	99,257,662,411	03	4,194,484,028	37	4 22
1910	50	102,553,959,069	28	4,195,293,966	90	4 09
1911	67	92,420,120,091	67	4,388,563,113	05	4 74
1912	65	96,672,300,863	67	5,051,262,291	57	5 22
1913	64	98,121,520,297	15	5,144,130,384	69	5 24
1914	62	89,760,344,971	31	5,128,647,302	16	5 71
1915	63	90,842,707,723	90	5,340,846,740	16	5 87
1916	63	147,180,709,461	18	8,561,624,447	46	5 82
1917	62	181,534,031,387	84	12,147,791,432	60	6 69
1918	59	174,524,179,028	72	17,255,062,671	17	9 88
1919	60	214,703,444,468	43	20,950,477,482	92	9 75

Totals. \$3,317,819,113,123 32 \$182,052,943,032 11 5 48%

Form 14 (continued)

## CHAPTER V

### COLLECTION OF TRANSIT ITEMS

#### Method of Collecting

The transit operations are those whereby the bank converts its country or out-of-town cash items into usable funds. As a business service the bank undertakes to receive and to give immediate credit to the depositor for cash items drawn upon banks located anywhere in the United States. From the standpoint of the depositor a transaction of this type is a valuable business service in that he is enabled to exchange an item payable at a distance for credit available at his local bank. Having received items of this sort and granted depositors the right to draw against them, the bank is confronted with the problem of obtaining funds in exchange for them upon the most favorable terms. Concretely, effecting an exchange upon "most favorable terms" consists of obtaining acceptable funds with as little delay in time and at as small an expense as is possible. Acceptable funds comprise (1) remittances in local funds (checks drawn either upon itself or upon clearing house banks), (2) credit with the federal reserve bank or with some correspondent, if the bank maintains accounts with other banks,<sup>1</sup> (3) reduction of its own deposit liability to correspondents.

To obtain these funds two methods are in use. The first consists in depositing the transit items with the local federal reserve bank for credit; the second consists in sending them to a correspondent bank for credit, as a charge against its account kept with the sending bank, or for remittance. The

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<sup>1</sup> Since the bank upon the practice of which this study is based does not maintain credit balances with domestic banks other than the federal reserve bank this phase of collections will be omitted from the discussion to follow.

first method results in increasing the bank's lawful reserve with the federal reserve bank, while the second method builds up a credit balance with a correspondent, reduces the bank's liability to its correspondent which effects the collection, or brings in a remittance in the form of local funds

### **Method in Use Before Passage of Federal Reserve Act**

Before the establishment of the federal reserve system two methods of collecting transit items were in operation. These were the clearing house method and the correspondent bank method.

### **Country Collection Department of Clearing House**

Under the clearing house method the local clearing house undertook to collect for its members transit items drawn on certain designated drawees. When the federal reserve system was established, it was realized that the activities of the country collection department of the clearing house were largely duplicated by the collection activities of the federal reserve bank. Accordingly after a short though successful career this department was dissolved.

### **Correspondent Bank Method**

The correspondent bank method of making collections, however, has survived the establishment of the federal reserve system. In following this method the bank maintains mutual connections with correspondents to which it sends and from which it receives items for collection.

Before the passing of the Federal Reserve Act this scheme was intimately connected with the reserve plan of the national and state banks. The out-of-town bank was permitted to count deposits with a New York bank, among others, as legal reserve against deposit liability, and in sending its checks drawn upon banks located in New York City or vicinity to

its New York correspondent it accomplished the dual purpose of building up its lawful reserve and collecting a portion of its country items. In addition to these advantages the out-of-town bank received a sizable rate of interest upon its New York balance, it had the privilege of selling New York drafts at a favorable rate of exchange, and it could count items sent to its city correspondent as lawful reserve from the time of mailing them, rather than after they had arrived in the city and had been collected by the correspondent. In many instances the out-of-town bank assessed profitable rates of exchange against items sent to it reciprocally for collection by its New York City correspondent.

In return for all these advantages which it offered to country banks the New York bank required the former banks to maintain balances of a certain size with it, and its advantage came from the use which it could make of these balances in its loaning operations. Under this system the securing of an out-of-town account by the New York bank often depended upon the character of the collection arrangement which that bank could offer.

Various forces have been in operation to lessen the scope of this system. Before the inauguration of the federal reserve system the clearing house abolished the practice which prevailed among some of its members of receiving all out-of-town deposit items at par by requiring each member to assess a minimum exchange charge against each country item which it received. Then too, the passing of the Federal Reserve Act marked the passing of the reserve-holding function from the national banks. At the same time the federal reserve banks undertook to effect collections of certain classes of country items for those banks which cared to have them do so. The scope of this system has been so widened that a majority of the country items received by a bank may be collected in this way, and since it offers member banks a convenient

means of building up and maintaining the lawful reserve they must keep with the federal reserve bank, the system is extensively used. Furthermore, the New York Clearing House Association narrowed the significance of the option which its member banks enjoyed of collecting through correspondents. This was done by passing a rule which in substance stated that no member bank would be permitted to pay a higher rate of exchange to a correspondent than it would be required to pay to the federal reserve bank for the collection of those items which the local federal reserve bank was willing to handle. As a result of the operation of these forces the system of collecting country items through correspondent banks has become secondary in importance to that of collecting them through the federal reserve bank. The correspondent bank system is still an important means of effecting collections, however, and in some cases is the only one available, since items drawn on certain points cannot be collected through the federal reserve banks.

The collection arrangement with out-of-town banks is effected at the time the account is opened and is changed from time to time as the two parties to the agreement see fit. The transit department of the bank receives and files these agreements as the officers of the bank report them. In general the out-of-town bank agrees to receive items drawn upon specified banks, including those drawn upon themselves and upon other banks in their more or less extensive vicinity. Certain rates of exchange may be charged by the collecting bank, the correspondent agreeing to maintain a certain average balance on deposit with the city bank, and it may receive a certain rate of interest on this balance.

The city correspondent reimburses itself for items sent to the country bank at the time of forwarding the collection items in one of three ways: (1) by charging the deposit account of the country bank, (2) by charging the account

when a certain number of days have elapsed after forwarding the item, or (3) by requiring a remittance from the collecting bank after collection has been effected. These three ways of settling for the proceeds of collections are termed respectively the "charge," the "transfer," and the "remittance" methods. Taking all factors into consideration—not only the mere collection arrangement with an out-of-town bank, but also the character of the account in all its phases—it is the business of the transit department, the function of which is to collect country cash items, to see that the collection business of the bank is so distributed among out-of-town banks as to be mutually profitable to the bank and to those of its correspondents who desire to handle such business.

### **The Federal Reserve Bank Collection System**

The federal reserve system of making collections is based upon the fact that the federal reserve banks are legally constituted the correspondents of all member banks of the system. As such they hold a balance to the credit of each member. The logical extension of such a system is for the member banks to be permitted to build up their lawful reserve with the federal reserve banks by depositing their out-of-town checks with those banks for collection and credit. Thus extension of the system was made by the adoption of a compulsory intra- and inter-district collection arrangement among the federal reserve banks on June 1, 1916. By this act, together with an amendment adopted in June, 1917, member banks and others desiring to use the federal reserve system for the purpose of making collections are permitted to do so at their option.

Each federal reserve bank publishes a detailed monthly list of the items which it will undertake to collect at par. At the time of writing these consist of only clean items and they are restricted as to drawees to include the following. (1)

those drawn upon member banks of the federal reserve system, (2) those drawn upon federal reserve banks, (3) those drawn upon non-member banks which are members of the clearing house associations situated in the twelve federal reserve cities, (4) those drawn upon other banks which will remit at par. The banks mentioned in the last classification include those which, under the privileges conferred upon them by the June, 1917, amendment to the Federal Reserve Act, have agreed to remit at par for all checks presented to them by the federal reserve banks in return for the privilege of sending their country items through the federal reserve banks for collection.

In receiving items for collection the federal reserve banks act only as collection agents for the sending banks and assume no responsibility other than due diligence in forwarding the items promptly. They do not charge exchange upon the items which they collect, but they make the proceeds of the collection available for the use of the bank only after the time required for collection has expired. To enable banks to know the time of availability of items, each federal reserve bank publishes a list showing when the proceeds of items will become available for credit. The time of availability is based upon the mail time required to reach the drawee bank, plus the time required for the federal reserve bank making the collection to receive funds in return.

All points within the scope of the scheme are grouped on this basis of average mail time into divisions of immediate, one, two, four, and eight days' availability. In keeping with this plan the federal reserve bank gives the depositor bank credit for all items received in time to be collected that same day. For all other items it makes an entry crediting a special collection account of the sender at par, but such credit is not available as reserve or to pay checks until the period required for collection has expired.



An example will serve to clarify the operations of this scheme. Suppose a New York bank on any given day sent transit items amounting to \$70,000 to the federal reserve banks, this sending being made up of the following checks:

First National Bank of Brooklyn, Brooklyn, New York	. \$24,000
Bank of Detroit, Detroit, Michigan.	. . . 20,000
Hibernia Bank and Trust Company, New Orleans, Louisiana.	16,000
Exchange National Bank, Tulsa, Oklahoma	10,000

In accepting these items the Federal Reserve Bank of New York would credit the collection account of the New York bank for \$70,000, but upon the given day only \$24,000, as represented by the Brooklyn check, which is one of immediate availability if delivered before nine o'clock, would be put at the disposal of the sending bank as eligible for reserve and as available for drawing. Credit for the balance of the sending would be withheld until the several items became available. Thus on the second day after deposit the reserve account of the sending bank would increase by \$20,000, the amount of the Detroit, or two-day check, on the fourth day it would increase by \$16,000, the amount of the New Orleans, or four-day item, and on the eighth day it would increase by \$10,000, the amount of the Tulsa, or eight-day check.

### Methods of Collecting Through Federal Reserve Banks

In dealing with the federal reserve banks the bank handles items in two different ways. All items which are payable in the local federal reserve district are taken to the local federal reserve bank as a deposit. Items of this sort are classed as deposit items and a regular deposit slip is made out in duplicate to accompany them. To save time and eliminate duplication of effort, all other federal reserve items are sent directly to the federal reserve bank of the district in which the drawees are located. These items are termed "direct sendings." The sending bank requests the out-of-town

federal reserve bank to credit the account of the New York Federal Reserve Bank with the proceeds of the collection, and it encloses a form of advice (Form 15) to be filled out and sent to the latter bank when collection has been made. This form serves to confirm the charge which the New York Federal Reserve Bank made against the account of the collecting bank on the date of availability of the items. The sending bank also advises the local federal reserve bank of its action on a form showing its sendings of items to each out-of-town federal reserve bank by availability dates.

Items which out-of-town federal reserve banks cannot collect are returned to the Federal Reserve Bank of New York. The latter bank credits the account of the out-of-town bank for all such items received and charges them back through the clearing house to the bank for which collection was attempted.

### Gold Settlement Fund

Mention should be made at this point of the device used by the federal reserve banks in making settlements among themselves. By virtue of the transit operations of the various banks in the United States which use the federal reserve system in making their collections, as well as other interdistrict operations, each federal reserve bank is constantly accumulating claims against each of the other federal reserve banks, just as one city bank accumulates claims against other member banks of the clearing house. To settle these claims what amounts to a gigantic clearing house has been set up by the Federal Reserve Board at Washington. A clearance fund, known as the "Gold Settlement Fund," was established in 1915. The fund is carried in the United States Treasury as a special account of the Federal Reserve Board. Each federal reserve bank at the time the fund was originated was required to deposit \$1,000,000 in gold, gold certificates, or gold order

FOUR DAY POINTS			
REPORT TO		DATE SENT <u>July 20</u> 1921	
FEDERAL RESERVE BANK OF NEW YORK			
OF CASH LETTERS SENT DIRECT BY			
BANK <u>National City Bank</u> ADDRESS <u>55 Wall St.</u>			
TOTAL TO BE CREDITED OUR ACCOUNT ON <u>July 25</u> 1921			
SENT TO	AMOUNT	SENT TO	AMOUNT
ATLANTA, Country	401 43	TOTAL REMITTANCE FROM US	46,977 72
ALA	1 36	PITTSBURGH, Country	15,087 09
TEXAS	25 00	W Va	10,003 21
Ga.		BRANCH OF CLEVELAND	
BIRMINGHAM, Country	122 29	RICHMOND, Country	7,070 77
ALA.	58 54	Mo CAL.	
BRANCH OF ATLANTA		So CAL.	
CHICAGO, Country	1,350 55	W Va	
Miss Iowa Ill.	3 55	ST LOUIS, Country	3,308 80
Ind Wis	7 63	Ark, Mo	4,800 52
CLEVELAND, Country	5 89	Ill., Tenn	423 73
Ohio	20 13	Ind	
W Va.		DENVER, City	3,400 67
CINCINNATI, Country	44 67	BRANCH OF KANSAS CITY	
Ky		DALLAS, City	
Ohio		EL PASO, City	436 05
BRANCH OF CLEVELAND		BRANCH OF DALLAS	
JACKSONVILLE, Country	436 05	HOUSTON, City	44 67
Fla.		BRANCH OF DALLAS	
BRANCH OF ATLANTA		SAN FRANCISCO, City	20 13
KANSAS CITY, Country			5 89
Kans			1,350 55
Mo		PORTLAND, City	7 63
LITTLE ROCK, Country	3,400 67		3 55
Ark.	425 78	BRANCH OF SAN FRANCISCO	
BRANCH OF ST LOUIS		SALT LAKE CITY, City	25 00
LOUISVILLE, Country	4,800 52		100 00
Ind Ky	3,308 80	BRANCH OF SAN FRANCISCO	
BRANCH OF ST LOUIS		SEATTLE, City	58 54
MEMPHIS, Country	7,070 77		
Ark.		BRANCH OF SAN FRANCISCO	
Miss		SPOKANE, City	122 29
Tenn		BRANCH OF SAN FRANCISCO	
BRANCH OF ST LOUIS		TOTAL FORWARD	46,977 72
MINNEAPOLIS, Country	10,003 21	GRAND TOTAL—4 DAY ITEMS	93,248 86
Mich	401 43		
Miss	1 36		
Wis			
NEW ORLEANS, City and	15,087 09		
Country			
Miss			
BRANCH OF ATLANTA			

Form 15 Advice to Federal Reserve Bank of Direct Sendings (Size  $8\frac{1}{2} \times 13\frac{1}{4}$ )

certificates, in addition to an amount at least equal to the net indebtedness due to all federal reserve banks at that date

Each federal reserve bank keeps a balance in this fund at all times and this balance counts as a part of its lawful reserve. Every morning each federal reserve bank telegraphs to the board the round amounts due to each of the other federal reserve banks, and the next day the settling clerks at Washington adjust their debits and credits by book entries. Deficiencies in the fund which result from this operation are covered by deposit of additional gold, or certificates in the treasury or any sub-treasury, or by credit operations such as rediscounts with other federal reserve banks which have an excess balance in the fund. Thus the balances resulting from most of the transit operations of the banks of the whole country are settled in a most economical manner without the actual shipment of gold.

### **Organization and Routine of Transit Department**

The organization of the bank for making collections of cash items through the federal reserve bank and through out-of-town correspondents consists of a transit department, the work of which is to effect collections, and of a collection ledger department, the function of which is to record and to follow up transit items in the process of collection.

The work of the transit department may be divided into three separate parts

1. The collection of transit items.
2. The collection of "trusts"—items collectible through the city collection department of the clearing house
3. The computation of exchange charges and the recording of interest delays

The transit items include all those classed as "countries" in the work of the other operating departments and all the

"sights" save the large ones which are collected by the messengers of the city collection department. The transit department collects the trusts because they are closely related to the sights, and missorts as between these two classes can be most quickly and easily righted by having the same department in the bank handle both. These are the primary and essential functions of a transit department. The third function, that of computing exchange charges and recording interest delays, while incidental, is closely related to the collection of the transit items. These charges and delays arise chiefly from the collecting operations and accounting for them may be performed best by expert transit clerks.

The transit department receives the material for its work mainly from the receiving departments of the bank—the mail teller and the receiving teller—but items also come from the foreign tellers, the note teller, and the city collection department. Certain correspondent banks in the city also make use of the facilities of the transit department under a reciprocal arrangement whereby the bank collects out-of-town items for these correspondents and they in turn collect for it items drawn upon banks in their immediate vicinity. These correspondents send their country items to the note teller for credit as ordinary deposits (see page 164).

The various departments sort and forward their work to the transit department in keeping with an arrangement which has been evolved for the purpose of entering for collection on the day of receipt just as large a volume of items as is possible with a transit force of reasonable size. During the morning each department sorts and sends all its country items to the transit department. During the afternoon they divide the countries into two classes—the "small countries" and the "large countries." The former are held over to the next day, while the latter are sent to the transit department to be handled that same day. The sights are divided into

the same classes, but the large sights, as indicated above, are sent to the city collection department for collection by messenger.

### **Division of Labor**

In keeping with the inflow of its work, the transit department operates in three sections the night, the morning, and the afternoon sections. The night work is merely preliminary to the morning, but that of the morning is quite distinct from that of the afternoon.

### **Night Force**

The material upon which the night force works consists of the small countries which have been held over from the work of the preceding day, the night mail from the mail teller, the trusts, and certain hold-overs from the transit work of the preceding day. The federal reserve bank gives immediately available credit for items which are deposited with it before nine o'clock and which can be collected the same day. For most items deposited at a later hour, however, the sending bank must suffer loss of an extra day's availability. Accordingly in this section the main object is to prepare those items which are to be collected through the Federal Reserve Bank of New York in order that they may be deposited with that institution at the beginning of business the next morning. Items which are to be sent elsewhere are laid aside for the morning section.

### **Morning and Afternoon Force**

The morning force completes the work upon these left-overs (non-federal reserve items from the night section), but its main work comes from the mail teller. This consists of the country items, both large and small, from the morning mail. The afternoon section handles the items which the

receiving teller has received up to a certain hour, together with the large country items from all departments of the bank. Thus the work is arranged so as to enable the bank to despatch for collection upon the day of receipt a considerable part of the items contained in the day's receipts, thereby avoiding loss of interest, while the size of the working force and also the hours of labor are kept within reasonable bounds.

The forces are divided into units, each of which operates a rack. The items are first proved in batches and sorted according to the rack division. Each rack handles items payable in states of a definite group. The groupings of the states in the racks are made for the most part to conform to the groups contained in each federal reserve district, but in the case of near-by districts the volume of the work is so large that these districts are divided among the various racks.

### Sorting Material of Racks

In forwarding items for collection the bank sends them to its correspondents in all cases where they desire to handle the items under the terms which the bank is permitted to offer by virtue of the clearing house restrictions, all other items are sent to the federal reserve banks. Many of the correspondent banks desire that only those items which are drawn upon themselves be forwarded to them for collection, others desire the business of a whole city or community. Because the federal reserve banks do not handle all classes of items the bank maintains a correspondent in each large financial center in order that it may have complete facilities for collecting non-federal reserve country items.

The men at the racks sort their items according to collecting banks. The correspondents' rack spaces are arranged alphabetically and the rack men first sort to them whatever

items these banks are to receive. The items remaining are sorted to the federal reserve compartments. Each federal reserve bank and branch has two compartments. One of these is for material which can be collected by that bank on the day of receipt. The items making up this material are termed "federal reserve city items," since they are generally drawn payable in the federal reserve cities. The other compartment is for material which the federal reserve banks cannot collect on the day of receipt. The items contained in this compartment are termed "federal reserve country items."

Generally speaking, the clerks in charge of each rack are familiar with the routings of the items with which they come in contact. For reference, however, route books showing a list of the correspondents of the bank and the collection arrangements in effect with them, also the publications of the federal reserve bank showing the items collected by it, are kept for the states handled by each rack.

### **Letters of Transmittal**

After the work of sorting the items is completed the rack men prepare letters of transmittal. These letters, which are prepared in duplicate, give the name of the sending bank, a list of the items which are enclosed, and instructions as to protest, wiring fate, etc. The letter sent to correspondent banks (Form 16) is printed on different colored paper according as the items are sent on a remittance, a charge, or a transfer basis. Letters for the federal reserve banks are made out on different forms, according as the items are sent to the local federal reserve bank as a deposit, or are a direct sending to other federal reserve banks or their branches. The carbon copies of these letters are retained in the bank. In addition to giving a list of the items enclosed, these carbon copies contain the names of the last indorsers of the items for convenience in tracing them should difficulties arise.



## Universal Transit Numbering System

Formerly it was necessary to write the full name of the drawee bank in listing each item on the remittance letter. In 1910, however, the transit managers from a number of

### THE NATIONAL CITY BANK OF NEW YORK

We enclose for collection items as listed below

UNLESS OTHERWISE INSTRUCTED - Do not hold collections for the convenience of parties.  
Surrender documents attached to drafts only on payment of same. PROTEST and RETURN  
without delay all dishonored paper. Telegraph non payment of all items over \$500

DO NOT PROTEST ITEMS \$10.00 OR UNDER.

To

CITIZENS AND SOUTHERN BANK  
SAVANNAH, GEORGIA.

10/28/21 FOD

64 808	45.67
64 356	123.42
64 732	234.87
64 892	134.73
BANK OF VIENNA, VIENNA GA.	1.01
PEOPLES BANK, SUMMIT GA.	5.87
	545.37c

Do Not Protest Items bearing the symbol (N P 18), or a similar authority of a preceding endorser

Form 16 Remittance Letter to Correspondent Bank (Size 6 x 7)

the leading clearing houses of the United States, under the auspices of the clearing house section of the American Bankers Association, devised a system of numbering the banks of the country for transit purposes. This system, called the

"universal numerical system," was adopted by the association in 1911. Under this system every bank in the United States has a distinctive number which is given in a directory, or key, published by the association.<sup>2</sup>

The system is used in varying degrees by the different banks, but it reaches its maximum usefulness only when all checks, drafts, and indorsement stamps of a bank bear that bank's transit number. A bank desiring to list a check drawn upon that bank would then be enabled to use the transit number, otherwise the effort required to look it up in the key would preclude such use. Thus a bank having occasion to refer to a check drawn upon the National City Bank of New York would find 1-8, the transit number of this bank, printed on the check and it would use that symbol instead of the name of the bank.

### **Mailing Transit Items**

The items to be enclosed in the letters of transmittal are indorsed after the usual form, i. e., making them payable to any bank or banker and guaranteeing previous indorsements. The letters are then made up and sent to the outgoing mail department for mailing. A self-addressed post-card for use of the collecting bank in acknowledging receipt of items is forwarded with each outgoing letter of the charge or transfer type.

### **Disposition of the Duplicate Letters—Charge Basis**

In the meantime the duplicate letters have been proved against the charges which were made against the given rack by the sorting desk. A duplicate letter representing items sent to a bank on a charge basis becomes a charge against that bank's account. These duplicate letters are sent to the

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<sup>2</sup> See "Key to the Numerical System of American Bankers Association," Rand McNally and Company.

customers bookkeepers, where they are charged to the accounts of the collecting agents and later filed for future reference

### **Letters Sent on Transfer or Remittance Basis**

Items sent out for collection on a transfer or a remittance basis obviously cannot be charged to the deposit account of the collecting agent on the day of transmission. The bank, however, has disposed of items of value and must make an entry to show for them. To meet this need special collection accounts are set up for each bank to which items are sent on a transfer or a remittance basis. Ledgers containing these accounts are kept by the collection ledger department. In sending out letters of this sort the transit clerks charge the items to the collection ledgers on their back proofs. The duplicate letters are forwarded to the collection ledger bookkeepers who enter them to the debit of the proper collection accounts.

Collections sent out on a transfer basis must be charged off the collection ledger and to the deposit account of the correspondent bank after a certain number of days have elapsed. The collection ledger bookkeepers, consequently, keep a careful watch over maturity dates of transfer items. As the required time elapses charge tickets are made out transferring the charges from the collection ledger to the customers ledgers. These tickets are sent through to the customers bookkeepers who charge the amounts to the deposit accounts of the collecting banks.

As remittances covering collections sent out on a remittance basis come in to the mail teller's department (see page 29), the letters are sent to the collection ledger department where they are credited to the collection accounts of the remitter. The transactions are then closed. Some banks remit the proceeds of collections when the collections are made, but it is quite a common arrangement to hold them until a prearranged

date for settling arrives, say semiweekly, and remit at one time for all collections which have been made for the whole period. It is an important function of the collection ledger bookkeepers to keep a watch over all such incoming remittances. If remittances are not forthcoming on time the unpaid item is followed up until the transaction is complete.

From the above it is apparent that the collection ledgers of the bank are books of control over cash items in the process of collection. The balance outstanding appears in the balance sheet of the bank in the account "Due from Banks and Bankers—Domestic."

Original letters of transmittal for items collected through the federal reserve banks are sent both to the New York Federal Reserve Bank and to the out-of-town federal reserve banks and branches in the usual way. Several letters are combined upon one deposit slip, however, in the case of those items which are sent directly to the local federal reserve bank, and the records of the bank with the federal reserve bank are kept by deposit slips rather than by individual letters. The duplicate letters for items of immediate availability are charged to the "Lawful Reserve with Federal Reserve Bank" account, while the ones of deferred availability are charged to a "Federal Reserve Bank Collection" account which is kept by the general bookkeepers. The general bookkeepers are charged with the duty of transferring these outstanding collections to the Lawful Reserve account as they become available.

### Collection of Trusts

The term "trusts" is a misleading one to the lay reader. Ordinarily one would think of trusts as signifying items drawn upon trust companies located in the city. However, in the classification of cash items used by the bank upon the practices of which this study is based, the term has no such sig-

nificance It refers rather to items drawn upon institutions which are reached by the city collection department of the New York Clearing House.

By a resolution adopted in 1917 the clearing house association began to make collections of items drawn upon certain non-clearing bankers, individuals, firms, and corporations for its members The association has made a list of selected institutions upon which it will present items for collection In preparing this list the object was to select those non-clearing institutions against which the heaviest collections were to be made by member banks.

Acting in conformity with the privileges extended under this resolution, the bank uses the clearing house to collect the trusts received before ten o'clock (the closing time for the entry of collection items at that institution). The whole mass of items which the bank desires to collect in this way is sorted according to drawees and those for each are placed in an envelope to which is attached a list indicating the contents, according to the clearing house requirement The clearing house association provides a regular form of route sheet upon which is entered the amount to be collected from each drawee bank and the total to be collected from all the banks on the given day These items are delivered at the clearing house and a receipt is obtained for them

The city collection department of the clearing house assembles the items it has accumulated from the sendings of the various member banks and delivers them to the various drawee banks It obtains checks drawn upon clearing house banks in payment for such items At the regular session of the clearing house at ten o'clock next day the collecting bank presents its receipt for the clearing house collection items which were delivered by it on the previous day, and clears the receipt in the regular way In exchange the clearing house collection department returns to the member banks items which are

refused by the drawees and it clears the checks which it has received from the drawee institutions

The transaction of collecting trusts thus brings into the bank clearing house funds which are available on the following day. At the close of the day these collection receipts are charged to the city collection department to be contained in the proof of the latter overnight, and in the morning they are sent to the mail teller for clearing.

### Departmental Proof

Proofs of the work of the transit department are made for the combined night and morning sections and for the afternoon section. The incoming items are proved by batches at the sorting desk. By keeping record of the incoming credits to the various tellers and departments of the bank, the proof clerk makes up the credit side of his sectional proof. The rack clerks each prepare a proof of their carbon copies of the letters of transmittal. These rack proofs are combined into scratch proofs which show the debit distribution of the items of the section as to the customers ledger groups, collection ledger groups, and federal reserve banks, the latter by classes of items as to availability.

The departmental proof (Form 17) is a combination of the two sectional proofs. In this proof the credit to the city collection department appears larger than might be anticipated from what has thus far been said about the relation of this department to the transit department. The city collection credit arises from the arrangement in vogue in the bank whereby all items held over from one day's work to the next are charged to the city collection department overnight. The departments receiving such items in their work on the next day then credit that department. The transit department's credit represents the small countries and the trusts held over from the preceding day.

## NATIONAL CITY BANK OF NEW YORK

Transit Department Proof, *May 2 1921*

Cut \$	603,485.16			2nd Tell. through 3rd Teller		715,650.58
" "	25,509.84			3rd Teller through 4th Teller		35,722.15
	32,778.18			For Ex. Dept. through 3rd Teller		13,645.04
	40,316.83			Rate and Trans. 3rd Teller		
	341,687.05			No. 43*	11,404.15	
				No. 44*	120,231.78	
				Columbus Bank*	32,990.63	
				" Branch*	17,057.65	
				Columbus Nat. Bank*	3,029.14	156,713.89
Bank of Ala. Ala. Ids	7,146.74			4th Tell. through 3rd Teller		248,219.69
Id. Kan.	3,181.82			4th Teller		2,834,116.85
Ky. Minn.	1,871.46					
Mo. N. Y.	1,644.91					
N. C. Okla.	625.41					
Ors. Tenn.	702.84					
Tex. Wyo.	1,917.52					
				2nd Teller	47,993.38	
				3rd Teller	33,099.66	
				4th Teller	866,268.65	947,361.69
STATE BANKS-TRUSTS SAV				(TOTAL)		3,051,479.26
Ala. Mo.	3,978.71			2nd Teller		3,524,142.33
Ill. Ind.	4,706.18			3rd Teller		184,238.59
Ind. Kan.	6,969.47			4th Teller T. M.		833,492.82
Ky. Minn.	216.34			5th Teller		
Mo. N. Y.	134.14			Foreign Exchange		2,283.71
N. C. Okla.	2,391.04					
Ors. So. Dak.	8,623.43					
Tenn.	1,003.37					
Texas Wyoming	579.15					
Dep't of Int. with Federal Reserve Bk. National Reserve Bank C. Jackson, Mo.	3,812,647.73					
	3,305,636.64					
Dep't of Foreign Banks-Canada						
"	1,236.06					
"	3,420.11					
"	3,822.47					
Charged to 3rd Teller	12,728.80					
A. M. Minn.	30,334.36					
P. M. Minn.	135,484.48					
Miscellaneous	1,448,606.51					
Total				Total		11,595,641.36

\* Banks for which this bank handles transit items, see page 108

Form 17 Transit Department's Daily Proof (Size 12 x 15.)

### Sundry Reports

In addition to proofs of the day's work the transit department prepares certain reports for the general bookkeepers and for the local federal reserve bank. A list of the charges passed to the various customers ledgers on account of items having been sent out on a charge basis is forwarded to the general bookkeepers' department in order that they may check the work of the customers bookkeepers. The general bookkeepers also receive reports of items sent to the collection ledgers and of those sent to the federal reserve banks, as indicated previously.

A report of the changes which have been made in the bank's reserve account due to the transit operations is sent to the cashier of the bank. A report of all direct sendings to federal reserve banks and branches is also prepared for the New York Federal Reserve Bank. This report contains one sheet for each class of items (those sent to one-day, two-day, four-day, and eight-day points) and a recapitulation sheet (Form 18) showing the total direct sendings by days of availability of the credits. Each sheet is prepared on paper of distinctive color.

### Assessment of Exchange Charges

The rules of the New York Clearing House Association determine the procedure of the bank in making charges for exchange. These rules divide all items into two classes: charge items for which the member bank must assess exchange charges, and discretionary items for which it may or may not do so at its discretion. For the guidance of members a table of charges is prepared classified by (1) checks or drafts drawn upon banks, bankers, and trust companies, (2) bankers' acceptances, and (3) all other items further classified by states. This table shows charges upon each class of items. A minimum charge of 10 cents is, however, fixed for each



FEDERAL RESERVE BANK  
OF NEW YORK

## RECAPITULATION

## CASH LETTERS SENT DIRECT

Date OCT. 28 19 31.

## REPORT TO

FEDERAL RESERVE BANK OF NEW YORK

## FROM

NATIONAL CITY BANK OF NEW YORK

Name of Bank

55 WALL STREET, NEW YORK CITY

Address

Of Cash Letters sent direct to other Federal Reserve Banks as per detailed lists attached  
hereto

Total of Letters to One Day Points	\$ 3,214,658 56
Total of Letters to Two Day Points	\$ 886,470 56
Total of Letters to Four Day Points	\$ 146,357 70
Total of Letters to Eight Day Points	\$ 41,810 99
<b>GRAND TOTAL</b>	<b>\$ 3,087,987 81</b>

NOTE—Credit will be given on the respective dates for the total available each day as  
shown above

It is very important that the separate total of each letter sent be shown. Do not show a  
total sent to any one bank that includes more than one letter

Please be particular to see that all figures reported are correct and are entered in the  
proper places

KEEP A COPY OF THIS REPORT FOR YOUR OWN FILES

deposit of items not classed as discretionary. These charges range from discretionary to one-quarter of 1 per cent and in general they are based on the mail time required for collecting the item. Charges for bankers' acceptances, especially, are based upon the time required to collect them, since according to the rules they are to be charged for according to rates derived from the current schedule published by the local federal reserve bank.

The transit department is charged with the duty of assessing exchange charges in accordance with those provisions. Accordingly all items receive the attention of exchange clerks before being sorted into the rack divisions. It is the policy of the bank to make no charge upon items designated as discretionary by the clearing house association. All charge items, however, are entered upon exchange sheets of which there is one for each depositor of the bank. These sheets show the date, place where item is payable, the face of the item, and the amount of exchange assessed. At the end of each fiscal month these columns are footed and a bill covering the charges is prepared for the customer as shown in Form 19.

Charges for exchanges are paid in one of three ways according to the desires of the customer. Some customers wish to pay exchange at the time of making their deposits. In this case the receiving teller accepts the amount, credits the note teller, and reports the fact to the transit department to avoid the making of a double charge. (See page 17.) Other customers desire to pay exchange in cash at the end of the month. This class of customers is accommodated by the note teller. The transit department makes charge entries in the accounts receivable exchange book, charging each customer's account receivable with the amount assessed against him and crediting Exchange account. When the note teller receives payment of a customer's exchange bill he credits that customer's Accounts Receivable Exchange account and stamps

THE NATIONAL CITY BANK OF NEW YORK			
Exchange Account With			
Name <i>J. K. Andrews Co</i>			
<i>New York City</i>			
Month: <i>April</i> - 1921			
26			10
27			12
28			
29			
30			
31			45 50
1			
2			12
3			
4			
5			26 10
6			
7			70
8			45 00
9			12 14
10			
11			
12			
13			
14			
15			16 17
16			10
17			
18			
19			13 00
20			
21			8 96
22			
23			
24			4 25
25			
<i>William F. McLaughlin</i>			
Dr Acct		174 31	

Form 19  
Bill for Exchange Charges to  
Customer (Size 11 x 3½)

THE NATIONAL CITY BANK OF NEW YORK			
TITLE OF ACCOUNT <i>Western Produce Co</i>			
CITY <i>Chicago Ill.</i>			
STATE <i>Ill.</i>			
The daily total of your items in process of collection upon which we delayed interest during the month of <i>April, 1921</i> is shown in the following schedule			
DATE	AMOUNTS		
	DELAY 1 DAY		DELAY 2 DAYS
	THOUSANDS	CENTS	IN CENTS
26			2 900
27			
28			
29			900
30			1 300
31			
1			4 800
2			1 000
3			1 600
4			
5			
6			7 000
7			4 600
8		2 000	
9			
10			7 700
11			8 900
12			
13			
14		8 000	7 800
15		1 000	15 200
16		3 000	1 100
17			1 000
18			4 000
19			5 000
20		3 000	1 500
21			
22			4 00
23			14 800
24			500
25			800
Totals	17 000		83 000
Total delay as of 1 day...		X 2	
		166 000	
		17 000	
		183 000	
TRANSIT DEPT			

Form 20  
Statement of Interest Delays Sent to  
Customers (Size 11 x 3½)

the date of payment opposite the amount paid. The third and most common class of customers have their exchange bills charged to their accounts by the bookkeepers. The statement of the transit department in such a case is sent to the bookkeepers who make the charge to the proper account and the bill appears among the vouchers returned to the customer.

### Interest Delays

When a customer to whom the bank pays interest on his balances, deposits items which cannot be immediately collected and used by the bank for loaning purposes, care must be taken to eliminate these unavailable items from the balance upon which interest is computed. If exchange charges have been assessed it is assumed by the bank that these charges compensate for the loss of interest, hence no interest delay deduction is made for items drawn on non-discretionary points which of course have been charged for under the clearing house rules. On all other unavailable items interest is delayed for a period corresponding approximately to the time required for collecting each particular item through the federal reserve bank.

Interest delays on items received by the mail teller are computed by a transit clerk attached to the mail teller's department. This clerk indicates on each incoming letter the proper interest delay. The bookkeepers who post the letters also have the duty of preparing daily balances for interest purposes, and by referring to the delay stamp they make the necessary deduction for the mail teller's unavailable items.

Deductions for items received by the receiving teller are computed in the transit department at the time of computing exchange charges. The country checks pass through the transit department where lists showing the delay to be made for each item drawn on a discretionary point are prepared. Delays on sights and trusts received by the receiving teller,

however, are not computed from inspection of the items themselves since the large ones do not pass through the transit department. The receiving teller submits to the transit department a list of all such items passing through his work, and this list becomes the basis for the computations of delays.

At the close of the interest period the lists showing interest delay for each customer on items deposited with the receiving teller are submitted to the interest department which makes the proper deduction. The transit department also prepares and mails to each customer a list showing all the items upon which interest has been delayed by the bank for the given period, as shown in Form 20.

### **Data for Analyzing Accounts**

For purposes of analyzing an account it is essential that the bank know the amount and cost of the collection service which it is furnishing gratuitously to the depositor. Accordingly a record is kept of the discretionary items collected for each depositor. In a separate section of the exchange sheets the face amount of each discretionary item or the total and number of small ones contained in a given deposit is entered, and in other columns the amount collected is entered under the time required to collect it. At the end of the month the completed exchange sheet is passed to the analysis department of the bank where it serves as a basis for their calculations made in this department.

### **Checking Incoming Bills for Exchange**

Because of its intimate knowledge of the arrangements in effect between the bank and correspondents which act as collection agents for it, the transit department is given the duty of checking the accuracy of bills for exchange charges rendered against the bank by its correspondents. These bills are checked against the duplicate letters and against the agree-

ments which are in force between the two banks; then their payment is authorized. A knowledge of the charges which are being made against the bank acts as an incentive to the transit clerks to route their sendings in a way to reduce such charges to a minimum.

### Summary of Transit Operations

The transit operations result in the collection of the country cash items and certain city items which cannot be collected through the clearing house. The collection of the items themselves results in three changes in the financial position of the bank: (1) actual funds are received from those banks to which items are sent on a remittance basis, (2) the bank's deposit account with the federal reserve bank is increased by the amount of the items collected through the federal reserve banks and branches, and (3) the deposit liability of the bank is reduced by the amount of the items which are sent to correspondent banks on a charge or a transfer basis.

## CHAPTER VI

### CITY COLLECTIONS

#### Collection of Cash Items

Thus far the discussion has traced the course of cash and cash items after they are received by the bank and the latter are converted into usable funds. It has been shown that the money received enters the paying teller's department, the clearing house checks go to the clearing house for collection, while the sights, trusts, and country checks are sent through the transit department for collection by the federal reserve bank, the city collection department of the clearing house, or correspondent banks.

These foregoing operations have accounted for all cash items received save the large sight drafts, the checks drawn upon the bank itself, and a few special items payable in the city but not taken by the federal reserve bank. The checks which are drawn upon the bank itself do not require any process of collecting. Accordingly there remain only the large sights and a few special cash items to be considered to make the collection of cash or deposit items complete.

It is impracticable, however, to pursue further the plan of following the course of cash items exclusively through the bank. Collection of the few remaining ones is effected by messenger or "by hand"; that is, messengers of the bank present them to the various drawees and receive acceptable funds in payment. The city collection department of the bank handles such collections but it devotes only a small portion of its time to these activities. To prevent duplication of effort it collects in addition to these cash items every other item payable in the city which cannot be sent through the

regular clearings, the city collection department of the clearing house, or the local federal reserve bank. These items are rather varied in nature but in general they are of two classes: (1) collection items, and (2) dishonored and rejected items.

### Collection Service

A very extensive service of the bank consists of making collections for its depositors and other customers. The collection service very closely resembles the cash item deposit service which has just been described in the preceding chapters. In fact the distinction between receiving items on a cash basis and receiving them on a collection basis arises largely from the method of handling the items within the bank itself rather than out of service performed. In most cases the collecting operations build up deposits in the same manner as do the cash operations.

There are important differences with respect to the way in which collections build up deposits as compared with the cash item operations. The cash item is immediately credited to the customer's account regardless of the fact that in many cases the bank must consume time in reimbursing itself for the advance which it makes to the depositor. In the handling of collection items, however, credit is made to the depositor's account or a check issued to him only after the bank has possessed itself of funds in return for the item offered for collection.

There are also some differences between the kind of items which make up the cash work and those entering the collection process. In the first place, items regarding which there is relative uncertainty as to their collectibility are not taken on a cash basis. In the second place, items requiring special service which is not provided in the ordinary process of collecting cash items, i.e., wiring advice of payment, etc., are generally accepted on a collection basis. Finally, the cash



work contains only sight, demand, and other items which have matured, while in the collection work no discrimination is made against instruments which are not yet due

In undertaking to make collections for customers the bank does not become the owner of the item to be collected. It acts merely as the agent of the owner. As such, it agrees to use ordinary care and diligence in attempting collection but beyond that point it is not responsible for any loss or disadvantage which may accrue to the owner of the item through its action. It is the policy of the bank, however, to devote the same care and attention to collection items that it devotes to its own cash items.

### Uses of Collection Service

The collection service of the bank has a threefold aspect. service, advertising, and revenue-producing. The bank considers it a necessary part of its service to make collections for its depositors. Accordingly the collection service is a gratuitous service for these customers, excepting in the case of foreign collections and of those out-of-town collections which must be charged for under the rules of the New York Clearing House.

The bank also uses its collection service as a device to attract new accounts. In this connection its collection facilities are made available to likely new business prospects on the same terms as those enjoyed by customers.

The third use which is made of the bank's collection facilities is that of producing an income for the bank. For various reasons there are those who do not desire to make use of the complete services of the bank through the account relation but who, nevertheless, may consider the occasional or the constant use of the bank's collection services for a stipulated fee a good business proposition. In dealing with these customers the bank approaches them purely on a business basis. They

use the collection facilities and expect to be charged a fee in keeping with the value of the service

### **Miscellaneous Collection Activities**

The collection work of the bank includes another class of items which has not as yet been mentioned. These consist mainly of items which have entered the bank on a deposit basis, but which have failed of collection through the ordinary channels. They include:

1. Checks and drafts which are returned to the bank by out-of-town correspondents because they could not pay or collect them
2. Cash items drawn upon the bank which it refuses to pay
3. Items which have been sent in error to the cash item departments of the bank and to the clearing house

Once a cash item has failed of collection it usually enters the collecting departments where it is handled in much the same way as a collection item

### **City Collection Department**

The organization of the bank for the work of effecting collection of the items which have been described consists of a city collection, or fifth teller's, department, and a messenger's department

The main work of the city collection department, as its name indicates, is to effect the collection of items which are payable in the city. This work includes, first, the collection of certain cash items, and second, the collection of the city items received on a collection basis. In addition to effecting the collection of the material just mentioned it also secures the acceptance of time items which are drawn upon city drawees. Again, all cash items which fail of collection through the

clearing house, or the transit department, or which the bank refuses to pay at the check desk, are collected by the city collection department. Lastly, some miscellaneous work, consisting mainly of reouting the missorts and hold-overs from the cash work of the bank to the proper departments and of recording the hold-overs, is performed. Briefly stated, then, the function of the city collection department is to obtain funds for all items payable in the city which cannot be collected through the clearing house or the federal reserve bank with the exception of notes and coupons. These are collected by the note teller's department and the coupon collection department respectively.

### **Territory of City Collection Department**

The territory of the city collection department embraces all that which is not covered by the transit department and the clearing house for cash items, and by the country collection department for collection items. In the work of banks in most cities this department would make collection of items upon all city drawees which could not be reached by the clearing house. Owing to the size of New York City, however, and the exceptional facilities which exist here for effecting collections, the city collection department of the bank upon the work of which this study is based covers only a small portion of the Greater City. The transit department, acting through the city collection department of the clearing house, the New York Federal Reserve Bank, and certain of the bank's correspondents located in the city, collects many city items and thus relieves the city collection department of a large amount of work. The territory of the city collection department, then, is narrowed down to include only downtown New York. In addition to handling collections in its regular territory the city collection department is given the task of collecting large items—say those in excess of \$5,000

payable anywhere in the Greater City and in certain of the more important suburbs. While the city territory is thus comparatively narrow, it must be borne in mind that it includes the New York financial offices of a great many of the large business concerns in the country and the work is therefore quite heavy.

### Collection of City Cash Items

The city collection department collects those large cash items which cannot reach the transit department in time to be sent to the federal reserve bank for immediate credit on the given day. On such items the loss of one day's interest which would result if they were held over until the next day more than outweighs the expense of collecting them by messenger. In addition the department collects certain documentary drafts forwarded to the bank on a cash basis which the federal reserve bank and the clearing house do not undertake to collect for members.

The items for collection are indorsed with the "paid" stamp, sorted according to the routes followed by the messengers, and entered in duplicate on route sheets. The route sheet shows the name of the drawee and the amount of the draft. It also has spaces for indicating the fate of the items after collection has been made or attempted. The original sheet is retained by the sight draft clerk as a record of the items sent out for collection.

The material to be collected, together with the duplicate route sheets, is then turned over to the messenger's department. The messengers present the items to the drawees and obtain either payment or refusal of them. As the messengers return from their routes the fate of each item is entered upon the original route sheet. If remittances have been received, the kind of funds which have been obtained is indicated. If, however, payment has been refused, notation of the fact is

made in the "fate" column of the route sheet. The completed sheets thus contain information showing the result of each presentment made by the messengers. They are then filed.

### **Disposition of Dishonored Cash Items**

Whatever cash items are unpaid are immediately charged back to the customer in order to bring his balance down to proper proportions, since the items were originally credited to his account. These items are entered in a book showing the reason for non-payment, the name of the drawee, the name of the indorser to which the bank looks for reimbursement, the amount of the drafts, and their fate. The unpaid instrument is also protested through the bank's notary unless the indorser has waived protest, the account of the customer is debited and the Commission-Notary Fees account is credited for the amount of these protest fees. Instead of returning the item immediately to the indorser, the bank generally enters it upon a collection basis by transferring it from the cash section to the collection section. Collection on this basis is then attempted.

### **Source of Collection Items**

The main source of collection items is the mail teller's department. To assist the mail teller with the heavy morning mail, representatives from the city collection department call at the former department and receive the collection items which belong to their department. After the heavy morning work is completed the mail teller's clerks themselves send the collection items to the city collection department. After the instructions of the customer have been copied the letter is returned to the mail teller who acknowledges receipt of it. Another source for a comparatively large amount of material is the foreign collection import department which receives all collection items sent from abroad.

### Kinds of Items Collected

The items to be collected are rather heterogeneous in nature and the specific classes are too numerous to be mentioned at this point. The city collection department handles only sight, demand, or matured time items, mainly drafts which are payable within its territory. It effects the collection of arrival drafts, however, and these are in substance time drafts. The drafts are either clean or documentary. Documentary drafts are those accompanied by bills of lading, stocks, bonds, and other securities and negotiable instruments which are to be delivered to the drawees upon payment of the draft. When the documents accompanying the drafts are securities, the drafts are called "stock drafts." The clean drafts for collection consist as a rule of those which cannot be handled as cash items because some special service, such as allowing the drawee a discount from the face of the item, sending a special advice of the result of the collection, etc., is desired by the customer, or because the owner has no account with the bank.

The collections are divided into four classes:

- 1 Those the proceeds of which are to be credited to the customer's account
2. Those which are to be settled for by means of a cashier's check
- 3 Stock drafts
- 4 Foreign drafts

To a certain extent each of these classes of collections is handled separately.

### Recording Collections

Incoming collection items are first entered from the customers' letters upon record sheets or collection registers (Form 21) which contain the following information: date, indorser,

DATE	ENDORSE	DRAWEE	LETTER DATE	NUMBER NUMBER	AMOUNT	INTER	INSTRUCTIONS	DEPOSITION
4/27/21	Jones & Co Boston Mass	Bank of Montreal	4/26	1407	250.00	No	Sight Draft	Paid 4/27/21
"	Wells National Bank	John Doe & Co	4/24	7034	3,140.00	Yes	Documents-Receipts	Accepted 4/27/21
"	do	Norfolk & Co	"	1035	5,160.00	Yes	Wire Payment	Good 4/27/21
"	do	Stevens & Co	"	1026	2,000.00	Yes	Payable Draft	Good 4/27/21
"	Mechanics National Bank	Boyd & Smith	4/23	3131	2,400.00	Yes	Wire Non-Payment	Good 4/27/21
"	do	Boyd & Smith	"	3132	137.00	No	—	Paid 4/27/21
"	Piggs National Bank Washington, D.C.	Bank of Montreal	4/26	1408	4,030.00	Yes	Advance Non-Pay	Good 4/27/21

Form 21. Collection Register. (Size 15% x 12.)

drawee, date of customer's letter, his collection number, amount, instructions as to protest, etc., and a column for noting the final disposition of the transaction. One sheet is kept for each class of items mentioned in the preceding paragraph. When the transaction is closed these sheets contain complete details of the attempt made to collect, whether it be successful or not. They are, accordingly, filed in a binder as a permanent record of the collection work.

THE NATIONAL CITY BANK OF NEW YORK		
Dear Sir(s):		New York, <u>April 27, 1921</u>
Your account has credit for the following described items		
YOUR LETTER DATE	YOUR NUMBER	DRAWEE
4-26	407A	Bank of Montreal
		\$ 4,036.10
To		ALL ITEMS PAYABLE ABOVE 14TH STREET OR OUT OF TOWN ARE CREDITED SUBJECT TO FINAL PAYMENT
<u>Riggs National Bank,</u>		
<u>Washington, D. C.</u>		
		CITY COLLECTION DEPT
		BY <u>Wm. Smith</u>

Form 22 (a) Letter Advising Credit for Proceeds of a Collection (original)  
(Size 6 x 8)

From the collection register sheets a form letter of advice (Form 22) is made out in triplicate. This form letter contains the customer's letter date, his number, or in the case of foreign items the number which has been assigned to the item by the foreign collection import department, name of the drawee, amount of draft, and method of settlement for proceeds. After collection has been effected the original of this letter serves as an advice to the customer that collection has been made. The duplicate serves as a credit ticket, as the basis



THE NATIONAL CITY BANK OF NEW YORK			No.
			Date <u>April 27, 1921</u>
CREDIT the account shown in lower left hand corner			
Check Letter Date	CHECK NUMBER	DRAWEE	AMOUNT OF CREDIT
4-28	407A	Bank of Montreal	\$ 4,036.10
<div style="border: 1px solid black; padding: 10px; display: inline-block; width: 80%;"> CREDIT   Riggs National Bank,  Washington, D. C. </div> <div style="display: inline-block; width: 15%; vertical-align: middle;"> City Collection Dept. </div>			
Checked, <u>WR</u>			<u>W. Smith</u> Clerk

Form 22 (b) Letter Advising Credit for Proceeds of a Collection (duplicate)

THE NATIONAL CITY BANK OF NEW YORK			
OFFICE COPY			Date <u>April 27, 1921</u>
Record of credit as follows			
Date of Check Letter	CHECK NUMBER	DRAWEE	AMOUNT OF CREDIT
4-28	407A	Bank of Montreal	\$ 4,036.10
Credited to			
Riggs National Bank, Washington, D. C.			CITY COLLECTION DEPT

Form 22 (c) Letter Advising Credit for Proceeds of a Collection (triplicate)

for issuing a cashier's check, or as instructions to the foreign collection import department, depending upon the nature of the collection. The triplicate copy is checked against the customer's letter to verify its accuracy, this operation in effect proving the entries on the collection register sheets, since the ticket was prepared from them. The ticket is then filed as a record of the collection.

After entry of the collection items has been made they are recorded upon route sheets and sent out for collection by the messenger's department in the same way as the items in the cash work. Drafts with stocks and bonds attached are collected only by experienced messengers who make a specialty of handling instruments of this sort. After collection has been effected the items which the messengers have received become a part of the cash receipts, while the tickets crediting the accounts of customers are proved against the cash brought in by the messengers.

### **The Credit Journal**

The credit tickets for customers' accounts are entered in the credit journal a sheet of which is illustrated in Form 23. The purpose of a credit journal is to obtain control figures over tickets sent to the bookkeepers of the bank for which the offset is a debit to cash. There is a column for each ledger to which credit tickets are sent. Each credit ticket is entered in the column of the ledger to which it pertains. At the close of the day the totals of the columns are obtained and the resultant figures showing the credits to each ledger are sent to the general bookkeepers for the purpose of building up the control accounts for the customers ledgers. After the tickets have been entered in the journal they are forwarded to the bookkeepers for posting. Credit tickets to general accounts of the bank are entered in a single column of the journal and forwarded to the general bookkeepers. The total





of this column in the credit journal serves to prove the total of the tickets received by the general bookkeepers

### Settling for Collections

Settlement for the proceeds of collections is made according to the instructions of the owner. Depositors generally request the bank to credit their accounts for the proper amount. If the customer desires the proceeds to be handled in this way the credit ticket is sent to the bookkeeper for posting according to the method just described.

In settling for collections with those who are not depositors of the bank and with those depositors who instruct it to do so, the bank uses a cashier's check. The city collection department is not authorized to issue cashier's checks, the work being centralized with the note teller except in the case of those departments which use cashier's checks in very large volume. In keeping with this arrangement the checks needed for paying customers are obtained from the note teller upon requisition.

Mention has already been made of the fact that in addition to operating its city collection machinery for the convenience of its depositors, the bank uses such machinery to attract new business and to produce income. When a collection is undertaken for one who is not a depositor of the bank the proposed transaction passes through the credit department and then to the official group in charge of the applicant's territory for approval. Coincident with approving the transaction the officers fix the charge, if any, to be made for the service. After completing the client's commitment the city collection department reports the transaction back to the credit department and they send it to the officers in charge of the customer's territory who send the check in settlement of the proceeds. By this arrangement the officers are enabled to write the proper follow-up letters to new business prospects.

### Procedure on Non-Payment

In case an item is not paid the instructions of the customers are carefully followed. In the absence of instructions to the contrary the item is protested if over \$10, and for all those over \$500 a telegram is sent to the customer advising him that the item is unpaid and asking for instructions. Almost every collection item, however, is subject to some sort of instructions, either special or standing. Those who regularly use the collection facilities of the bank, file standing instructions which they desire to have the bank follow in the event that certain classes of items are unpaid. These instructions are filed away and carefully observed. In addition, special instructions covering a given item are generally contained in the letter of the customer and are entered on the duplicate advice slip for the guidance of the department. These instructions cover such points as protest, wiring or advising fate, holding against arrival of goods, etc.

After it has been definitely established that a collection cannot be made, the item is returned to the customer who reimburses the bank for protest fees and other expense which it has incurred. In general, however, every effort is made both by the bank and by the owner of the draft to have it paid. To close out special transactions of this sort, strictly non-banking functions are performed at times, but such service is furnished only in exceptional cases. The bank endeavors at all times to avoid transactions which carry it beyond its proper functions.

### Arrival Drafts

The collection service in connection with arrival drafts merits special consideration. An arrival draft is one accompanied by a bill of lading and made payable when the shipment covered by the bill of lading arrives at its destination. The bank presents a draft of this sort to the drawee on the day

of receipt This presentment, however, is merely for the purpose of notifying the drawee that the bank has the draft for collection Collection of the draft and surrender of the bill of lading will be made only when the shipment arrives The consignee can generally be relied upon to watch for the arrival of the merchandise and notify the bank of his willingness to take up the draft, since he is, presumably, desirous of obtaining his consignment as promptly as possible To make sure that the interests of its customers are being served, the bank sends the drawee each week a notice of the fact that it is holding the draft pending the arrival of the goods The owner is also advised that the draft is being held, a duplicate copy of the notice sent the drawee serving this purpose A third copy is retained as an office copy Notices of this sort are sent out regularly until payment of an arrival draft is made or refused by the drawee

Customers often negotiate short loans with the loan department of the bank upon the collateral of arrival drafts The bank, having previously ascertained the willingness of the drawee to meet such a draft upon the arrival of the goods, advances funds to the owner upon the security of the proceeds of the collection, backed up by the lien upon the shipment itself, afforded by the bill of lading In such a case the draft is held by the city collection department, but after collection is effected the transaction is sent to the loan department where the funds collected are used to pay off the outstanding loan The balance is then credited to the customer's account

### Acceptance of Time Items

In addition to its regular collection work the city collection department secures the acceptance of those time items which come to the bank drawn upon drawees within the city territory Items of this sort are entered upon a special collection register sheet and presented to the drawees They are, if necessary,

left in the possession of the drawee overnight for examination. If accepted the drafts are turned over to the note teller's department for collection at maturity, or to the discount department if they are to be discounted in accordance with the instructions of the owner. Items which fail to be accepted are handled according to the instructions of the drawers in much the same way as are regular collection items. Many drafts for acceptance, especially those from the foreign division, are accompanied by documents which are to be delivered to the drawees upon acceptance of the drafts. In this case the documents remain in the possession of the bank until acceptance is effected, but the drafts themselves may be left out overnight for examination by the drawees just as are clean bills.

### **Recovery of Uncollected and Dishonored Items**

In addition to the work of collecting city items, the city collection department has the function of making recovery on cash items which have failed of collection and for protest fees incurred in connection with dishonored cash and collection items. It also recovers on items which the check desk of the bank refuses to pay and redeems those which are returned to the bank from the clearings. Lastly, this department takes charge of all missorts to the other departments of the bank and of those held over from one day's work to another.

A collection return item is one which has been sent out by the bank to some correspondent on a collection basis and which is returned unpaid by the collecting agent. Such items come first to the mail teller's department where a credit is put through to the account of the collecting agent for such expenses as protest fees paid by him. This department routes all collection returns, save those upon which protest fees have been incurred, to the country collection department for return to the customer. Collection returns upon which protest fees have been paid are sent to the city collection department.



where the amount is recovered from the customer and the dishonored item returned to him

Cash return items are those which were forwarded to and later returned by federal reserve banks, correspondents, or the clearing house, because these agencies were unable to pay or collect them. The drawees of items of this sort may refuse to pay them because the drawers have insufficient funds on deposit, because of stop-payment orders, irregularities in body, forged or missing signatures or indorsements, etc. Again, the transit or the assembly rack department may have sent items to the wrong banks.

Out-of-town correspondent banks return these items to the bank through the mail teller together with a reason for the return of each. The mail teller credits the correspondent and charges the return to the city collection department. In addition to these returns from out-of-town banks there are clearing house returns which the clearing house banks return directly to the city collection department either by messenger or through the three o'clock session at the clearing house.

### **Clearing House Redemptions**

Items returned to the bank by clearing house members are redeemed by a distinctive form of cashier's check used by all clearing house banks, as shown in Form 24. These checks are made non-negotiable, except through the clearing house, and they are to be used only for the purpose of making redemptions. The redemption check covers in addition to the amount of the returned item the fine, if any, which the bank making the return claims under the clearing house rules.

The Fine account is debited for each fine which is incurred and a record is kept of the clerk who was responsible for the error. Once a month the balance of the Fine account is determined and a pro rata charge made against the salary of each employee who has caused fines to be charged against

[illegible]

the bank. No attempt is made to recover the full loss which has been incurred by fines, the idea being rather to provide a punitive device for reducing to a minimum errors due to carelessness.

### Cash Items Dishonored by Bank

The cash return items which are collected are augmented by the items which the bank itself refuses to pay. The customers bookkeepers and the signature control department act

<p><i>Returned to No</i> ... <u>54</u> ...</p> <p style="text-align: center; font-size: small;">BY</p> <p style="text-align: center;"><b>THE NATIONAL CITY BANK OF NEW YORK</b></p> <p><i>for reasons indicated below</i></p> <table style="width: 100%; font-size: small;"> <tr> <td style="width: 50%; vertical-align: top;"> <p>Guarantee Endorsement _____</p> <p>Missing _____</p> <p>Legible _____</p> <p>Bank Stamp _____</p> <p>Endorse as Draws _____</p> <p>Date Receipt _____</p> <p>Sign Receipt _____</p> <p>Sent Wrong _____</p> <p>Not Due _____</p> </td> <td style="width: 50%; vertical-align: top;"> <p>Payment Stopped _____</p> <p>Insufficient Funds _____</p> <p>No Account _____</p> <p>Signature Missing _____</p> <p style="text-align: center;">Unknown</p> <p>Date _____</p> <p>Filling _____</p> <p>Counter Signature _____</p> </td> </tr> </table> <p style="font-size: x-small;">These endorsements appear to be written by the same person. This check must be endorsed by each payee in his own handwriting.</p>		<p>Guarantee Endorsement _____</p> <p>Missing _____</p> <p>Legible _____</p> <p>Bank Stamp _____</p> <p>Endorse as Draws _____</p> <p>Date Receipt _____</p> <p>Sign Receipt _____</p> <p>Sent Wrong _____</p> <p>Not Due _____</p>	<p>Payment Stopped _____</p> <p>Insufficient Funds _____</p> <p>No Account _____</p> <p>Signature Missing _____</p> <p style="text-align: center;">Unknown</p> <p>Date _____</p> <p>Filling _____</p> <p>Counter Signature _____</p>
<p>Guarantee Endorsement _____</p> <p>Missing _____</p> <p>Legible _____</p> <p>Bank Stamp _____</p> <p>Endorse as Draws _____</p> <p>Date Receipt _____</p> <p>Sign Receipt _____</p> <p>Sent Wrong _____</p> <p>Not Due _____</p>	<p>Payment Stopped _____</p> <p>Insufficient Funds _____</p> <p>No Account _____</p> <p>Signature Missing _____</p> <p style="text-align: center;">Unknown</p> <p>Date _____</p> <p>Filling _____</p> <p>Counter Signature _____</p>		

Form 25 Slip Attached to Dishonored Clearing House Item. (Size  $4\frac{1}{4} \times 2\frac{1}{2}$ )

as a court of final jurisdiction as to what checks the bank will pay. It is the work of the signature control department to detect all forged, missing, or irregular signatures or indorsements and other irregularities affecting checks which make it advisable not to pay them. The bookkeepers guard against incurring overdrafts and paying checks against which stop-payment orders are outstanding. Checks of this sort together with those which have been sent in error to the bank through the clearing house are sent to the city collection department by the bookkeepers. This latter department attaches a slip (Form 25) to each clearing house item showing whether it

is to be returned by hand or through the clearing house, together with the reason for refusing to pay it.

### Cash Returns

Cash returns are collected by the city collection department in a manner depending upon the cause for return and in keeping with the means which are at its disposal for effecting such collections. If the cause for non-payment is that the item was missent either through the clearing house or by the transit department, the error is corrected by sending the item out for collection to the proper agent. Minor irregularities usually are corrected without recourse being had to an indorser.

In most cases of non-payment of cash items, however, collection will be impossible, and the bank looks to the depositor for reimbursement. It will be recalled that the bank reserves the right to charge deposit items back to the depositor's account in the event it is unable to effect collection. Returns of this sort are accordingly presented by hand to those indorsers whose places of business are within its territory and by mail to those located out of town. The former reimburse the bank in cash, while in dealing with the latter the bank charges their accounts for the face of the item together with protest fees. In returning an item by mail, duplicate charge tickets are used, one copy of which is sent to the customers bookkeepers as a charge to the customer's account and the other copy accompanies the item as a letter of advice to the depositor.

### Clearing House Returns

All "sent wrongs" and other items upon which the bank is entitled to collect a fine under the rules of the clearing house are returned to the offending bank by hand. These returns must be presented to the receiving banks before three o'clock, otherwise the fine cannot be claimed. Accordingly, as these

items are discovered by the check desk and charged to the city collection department they are at once forwarded by messenger for collection. All other items to be returned to the clearing house are sent, if possible, to the three o'clock clearing house session which is held solely for the purpose of returning items of this sort. Otherwise they are collected by hand. The Fine account is credited for all fines which are collected.

### Clearances and Redemptions

The city collection department also handles the clearances and the redemptions for certain city correspondents which use the bank as their clearing agent, the term "clearances" referring to the items presented at the clearing house against these particular banks. For example, say the National City Bank clears for the New York agent of the Bank of Montreal. Under an arrangement of this sort the various clearing house banks present their checks upon the Bank of Montreal agent to the National City Bank along with the checks drawn upon the bank itself, the Montreal checks received by the National City Bank are termed "clearances" in the work of the institution. These items are sent to the check desk as are the items received from the clearing house drawn upon the bank itself. The check desk delivers them to the city collection department which in turn delivers them to the drawee bank and obtains a check in settlement.

During the day the drawee banks for which the bank clears examine the clearances. The items which they refuse to pay they send to the clearing bank for reimbursement. Recovery from the offending banks is then obtained just as recovery is made for the items sent to the bank itself which cannot be paid. Likewise redemption of the sendings of these particular banks is attended to by the city collection department and reimbursement obtained from them.

### Missent and Hold-Over Items

A highly important function of the city collection department is that of acting as a depository for missorted and held-over items from other departments of the bank. It often happens that an item is sent from one department to another in error. These errors within the bank are corrected by charging the items to the city collection department, the latter department then throws them in with its regular cash items and sends them to the proper department for treatment. In a similar manner, to relieve the paying teller, the checks which he has cashed, excepting those which are drawn upon the bank itself, are sent to the city collection department and forwarded by it to the proper departments for collection.

The work of each department of the bank must close at an hour in keeping with rational working hours for employees. Hence in such departments as the mail, receiving teller's, transit, etc., there are certain cash items which have not been made ready for collection at the close of the day. These items are charged to the city collection department in order that they may be assembled upon one record, but the items themselves are passed on to the bank's various night forces where they are prepared for collection the following day. The city collection department thus becomes the agency in the bank for holding all the unfinished cash business of the operating departments on its records overnight, and for correcting errors arising within the bank in the passing of items from one process to another.

### Disposition of Receipts

The receipts of the city collection department are disposed of in the same manner as are those of other departments. The currency goes to the paying teller, the checks upon the bank itself go to the check desk, and the clearing house checks are prepared for collection by the assembly racks. The city

collection department does not accept country items, sights, and trusts in payment of the collections which it makes. Through the receipt of checks and drafts from the paying teller and missorts, however, some such items will have been obtained. These are routed to the transit department for collection. Charge and credit tickets resulting from the day's work are sent to the customers bookkeepers to be posted to the proper accounts.

### **Fifth Teller's Proof**

Several subsidiary proofs are prepared in the city collection department. A separate proof is made of the cash work, of the collection work, and of the returns. At the close of the day a general proof is prepared, as shown in Form 26. In addition to giving a condensed journal record of the transactions passing through the department for the day, this proof serves the highly important function of constituting an inventory of the unfinished cash work, since all unfinished items are charged to this department at the close of the day. This proof ranks with the other proofs of the bank in importance as a record of departmental activities and it serves the added function of showing an inventory of the cash work in process, just as the paying teller's proof in addition to giving a record of the work of his department shows the amount of actual cash on hand.

### **Messengers' Department**

As has already been indicated the work of making collections in the city by the city collection department is done "by hand," i.e., by messenger. The work of making these collections along with that of carrying money, securities, documents, and notices between the bank and such institutions as the bank's affiliated corporations, the clearing house, the federal reserve bank, and such clients as stock brokers, borrowers,

## FIFTH TELLER

[illegible]



etc., is heavy enough to require the services of a large messenger force. This force is grouped together into a specialized messenger's department

The demands which are made upon the messenger's department are uneven from hour to hour. From eight o'clock to ten o'clock the work is comparatively light. Between ten o'clock and three in the afternoon the work of the city collection, note teller's, coupon collection, and other departments demands that many errands be run. After three o'clock there is a let-up in the work. To meet this situation the messenger force is shifted about from task to task. In the morning the messengers assist the mail teller in handling the morning mail and the assembly racks. In the afternoon they are assigned to the various departments which may be in need of special messengers. In addition to keeping the messenger force profitably employed this shifting about trains the employees in the work of the bank and thus prepares them for advancement. In contrast to these, certain of the older and more experienced messengers are assigned definite tasks which they perform daily. For example, a special messenger attends to making gold shipments and to carrying large sums of cash between the bank and such institutions as the assay office and the federal reserve bank. Certain others assist the paying teller in tending the vaults and carrying large sums of money from place to place. Other special messengers handle stock drafts and other items of this sort.

### **Messengers' Routine**

In effecting collections each messenger travels a definite route and in general handles a special class of items. He receives his items against signature from the departments whose work he is assigned to handle and he is held responsible for all items which he signs for. In effecting collections the bank accepts only checks drawn on itself, upon clearing house

banks, or cash. As a general rule all checks of \$500 or over in amount must be certified. In case of payment against documentary drafts it is customary to require that all checks be certified. The rule as to certification, however, is disregarded in dealing with well-known, highly responsible drawees. Time items requiring acceptance are left in the possession of the drawees overnight for examination. The messenger prepares a "left-out" slip which is used by the bank to represent the item left out until it is "picked up" by the messenger the next day.

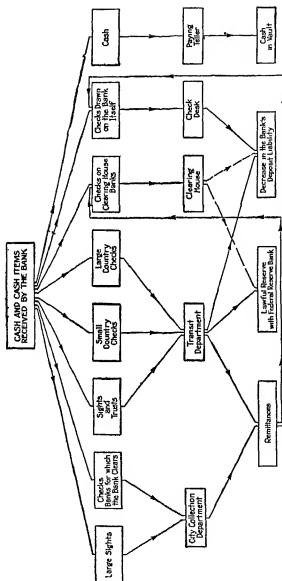
In case a messenger is unable to locate the proper party at his office, or in case an item is refused, a notice of present-

<b>THE NATIONAL CITY BANK OF NEW YORK</b> FIFTY FIVE WALL STREET	
Mr.	<u>Progar &amp; Drew</u>
A sight draft on you for <u>\$2,418<sup>00</sup></u>	
drawn by	<u>Henry S. Brown &amp; Co.</u>
regularly presented at your office for payment	
It will be held at this Bank (City Collection Dept.) until three o'clock this day Saturday until 12 o'clock only	
New York,	<u>April 27, 1921</u>
CITY COLLECTION DEPT. By <u>W. J. Smith</u>	
Our messengers have no authority to make promises or make instructions. Persons wishing to communicate with the Bank relative to this item must do so during business hours. If by telephone, call 7900. Messengers City Collection Dept. Checks intended in payment of drafts of \$100.00 or over or with documents must be certified.	

Form 27 Notice of Presentment (Size 7 x 3.)

ment (Form 27) is left at the drawee's office as evidence that presentment of the item has been made. The bank undertakes to hold the item for a short time to enable the drawee to call and pay it.

When the messenger returns from his route he reports directly to the department the work of which he is handling. The items which he brings back are carefully checked against the route sheets, each item taken out must be represented either by funds, a left-out ticket, or it must be brought back with reasons for non-payment.



Form 28 Chart Showing Disposition of Cash Items Received by the Bank

### Summary of City Collection Work

The work of the city collection department marks three achievements in the progress of work through the bank (1) the last items in the cash work have been collected; (2) the errors in the other cash item operations have been adjusted, and (3) the collection of non-cash items has been introduced. At this point other departments of the bank join with the city collection department to supplement the collection service of the bank.

A chart showing the disposition of all cash and cash items received by the bank (Form 28) summarizes and presents in condensed form the procedure described up to this point.

## CHAPTER VII

### COLLECTION OF NOTES, COUPONS, AND COUNTRY ITEMS

#### Note Teller's Department

The note, or third, teller's department is a collection department, but only in a general sense. Genetically, this department is the matrix from which sprung such departments as the city collection, the coupon collection, the messengers', etc. In the early history of the bank the note teller's department had the function of collecting all city items and of attending to the various miscellaneous teller activities which are necessary in any bank. As the bank grew to its present size, however, gradually the departments just named were evolved and they have assumed one by one the original collection functions of the note teller's department until only one—the collection of notes and acceptances for customers—remains. On the other hand the miscellaneous teller duties have been retained through all this evolution. The result is that the note teller's department has two functions (1) collecting notes and acceptances, and (2) performing miscellaneous teller activities.

#### Receiving Items for Collection

The collection work of the note teller's department consists of two separate and distinct parts. In the first place this department acts as a receiving teller for items which are being entered for collection by the local customers of the bank. Acting in this capacity it receives whatever items these customers of the bank enter for collection rather than for immediate credit to their accounts, obtaining instructions from

the owners as to how the transactions are to be handled. Receipt is given for the items on the last page of the pass book or upon a receipt form, according to the wishes of the customer. After this is done the note teller's department is not further involved in the transaction unless the item entered for collection be a note or an acceptance. The work is passed on to other departments of the bank as follows:

- 1 The coupons, to the coupon collection department
- 2 Out-of-town collections, to the country collection department
- 3 Items payable in the city, to the city collection department

### Collection of Notes

The second collection function of the note teller's department consists in actually effecting collection of and settling with the customers of the bank for notes and acceptances which have been entered for collection. This work of collecting notes and other time items is the primary function of the note teller's department. It is the one from which the department derives its name, although in a large bank some of its miscellaneous work may equal or even exceed the collection of notes in volume, if not in importance.

### Note and Acceptance Blotters

The first step in the process of preparing notes for collection is to enter them in blotters or collection registers. The note teller's department has a register in which are entered those notes and acceptances which are received over the window. For items coming from other sources, however, the departments which receive them keep the registers. Thus the city collection department keeps a register giving a record of the acceptances which it passes to the note teller's department for collection, and the registered mail department and

the mail tellers likewise keep blotters giving details of the notes and acceptances they send to the note teller's department. While the foreign collection import department does not keep a separate register covering its sendings of notes and acceptances, its records are designed to give the necessary information in another way.

The collection registers are merely designed to obtain control over incoming collection items of this sort and for the recording of essential information for guidance in making collections. They contain the following information: date of customer's letter, address of sender, indorser, customer's collection number, due date, instructions as to protest, where payable, amount, and special instructions.

### Timing the Items

To protect owners and indorsers in the event of possible non-payment, it is essential that the bank present notes and acceptances for payment on the exact due date. To assist in bringing about presentment for collection on the proper date, the due date of each item is determined and entered conspicuously in color on the face of the instrument. This process is called "timing." In order that a high degree of accuracy be obtained in the timing, two checkings of the work are made.

When the notes and acceptances have been timed a quadruplicate ticket is prepared for each transaction. This ticket contains the following information: date transaction was entered, name of owner, name of maker or acceptor, date of his collection letter, date payable, place payable, amount of the item, owner's collection number, and method of settlement for the proceeds. Any special instructions are also noted on the ticket. The original of the ticket serves as an advice of credit to the customer and is sent to him at the time collection is effected. The duplicate copy serves as a ticket crediting the amount collected on the note or acceptance.

to the customer's account or to the Cashier's Check account. These two copies are attached to the instrument which is to be collected and they follow it through the remainder of the work.

### **Owners' File**

The third copy of the ticket is placed in the owners' file. In this file the tickets representing the work completed during the last few months and that in process for each customer for whom the department makes collections are filed together. This file is particularly useful for referring to an item concerning which the owner makes inquiry. It is also useful for showing the amount of collection business transacted and pending for each customer, and at what time and how large accretions to his account may be expected in case the question of carrying an overdraft for him comes up for consideration.

### **Makers' and Acceptors' File**

The fourth copy of the ticket is filed in the makers' and acceptors' file according to the name of the one who is to pay. The purpose of this file is to indicate the collections made and pending against the various makers and acceptors from whom the bank makes collections. This file serves the important function of furnishing information regarding maturities in case makers or acceptors make inquiry regarding their obligations held by the bank. After collection has been effected the corresponding tickets remain in its files for a considerable period of time.

### **Ticklers**

After the proper tickets have been drawn the notes and acceptances are entered in the tickler. It is the function of the tickler to indicate the instruments which must have attention each day. This book is therefore divided into sections,



one for each business day, in each of which are entered all items falling due on that day. From these entries the department thus has a list of the notes and acceptances which it must collect as each business day arrives.

### **Note Boxes**

The final step in the process of preparing instruments for collection consists in filing them in note boxes. The purpose of the note boxes is to make the material of given maturity date readily available for attention. The note boxes are divided into two sections: one for filing items payable in the city, and the other for those payable out of town. Each section is divided into compartments each of which contains the notes of a given maturity date. The notes and acceptances recorded on each page of the tickler are thus contained in separate compartments, the country items in one section and the city items in another.

After the notes and acceptances have been entered in the tickler and filed in the note boxes the transaction lies dormant until the proper time for collection arrives unless, of course, the owner desires to withdraw his item or to make some other change in his instructions. The second and last phase of the collection process consists in effecting collection and accounting for the proceeds of items as the proper dates for presentment arrive.

### **Country Notes and Acceptances**

Notes and acceptances which are payable outside the city are collected by the country collection department. When such items are received they are prepared for collection in the same way as are city items. By means of the tickler the due dates of the country items held are ascertained. These items are sent to the country collection department about ten days before they mature, in order that this department may

have opportunity to put them for collection in the hands of an out-of-town correspondent by the time the due date arrives. The country collection department attends to the further details of effecting collection and making settlement with the owners.

### City Notes and Acceptances

In connection with notes and acceptances payable in the city territory the note teller's department follows the collection process through to completion. On the day before maturity everything is put in readiness to present items for payment. By means of the tickler and note files the notes and acceptances are readily brought to attention. The advices and credit tickets are separated from the instruments and they are proved against each other to make sure that the tickets have been made out correctly. The collections are entered in a route book according to the messengers' routes. Then to make sure that attention has been given to all details the credit tickets are checked against the route book and these two in turn against the tickler.

On the following day the majority of the notes and acceptances are sent out for collection by messenger. The messengers make presentment and demand for payment on the maker or acceptor and turn over the funds obtained or the dishonored items to the note teller's department.

### Collections Payable at Bank

An item made payable at the bank is not collected by messenger. It is customary to regard such items as payable by the bank on the date of maturity, just as a check drawn against the depositor's account. Accordingly, unless the maker or acceptor has instructed the bank not to do so, the note teller's department has the bookkeeper withhold from the account an amount sufficient to meet the amount of the collection.

The item itself is sent to the bookkeeper to be charged to the account along with the checks. Such a collection therefore involves merely a book entry if the balance of the maker or acceptor of the item is large enough to support the necessary charge. If the customer has not sufficient funds on deposit to meet his maturing obligation, the bank presents the item for payment to him by messenger or communicates with him in order that he may have opportunity to arrange to make payment.

### **Collections Payable at Clearing House**

Notes and acceptances, made or accepted, payable at clearing house banks are collected by presenting them through the clearing house to these banks. Should such items be presented in the usual way on the due date and be dishonored by the banks at which they are made payable, they would not be returned to the collecting banks until three o'clock in the afternoon. As a result it would be practically impossible to make demand on the maker or acceptor for payment on that day. To avoid this difficulty the bank on the morning of the due date presents items of this sort by messenger to the banks at which they are made payable. If the banks desire to pay the items they certify them and the collecting bank passes them through the morning clearings on the following day. If, however, the items are refused by the banks at which they are made payable, there yet remains time in most cases for the bank to make presentment for payment direct.

### **Settlement for Collection**

After collection has been effected the note teller's department makes settlement with the owner by crediting his account or by sending him a cashier's check, according to instructions. If instructions are to credit the owner's account for the proceeds of the collection, the ticket which was prepared when

the item was entered for collection becomes a credit ticket to the customer's account and it is sent to the bookkeepers for posting. If on the other hand the owner desires a cashier's check, the ticket is used as a requisition for the cashier's check and a credit ticket to Check account. The advice of payment which was prepared concurrently with the above-mentioned ticket is then mailed to the owner. The note teller handles unpaid collection items in the same way as does the city collection department, returning them to the owners together with a bill for protest fees, if any.

### Miscellaneous Functions

Aside from collecting notes and acceptances the note teller's department does the odds and ends of the teller work of the bank. According to the expression current among the clerks of the bank this department does everything which the other tellers and departments do not do. These functions are so heterogeneous in nature that no attempt will be made to classify them in more than an elementary way. Each one must be treated separately.

### Deliveries Against Payment

Occasionally customers send valuable papers, such as stock certificates, bonds, deeds, mortgages, notes, etc., which they instruct the bank to deliver to certain parties when these parties have made a payment to the bank for the account of the sender, or have performed some other specific act. Sometimes customers desire the bank merely to deliver documents of this sort, obtaining receipt from those to whom delivery is made. At other times the transaction may take the form of complying with a customer's request to sell rare coins or similar valuables which he has sent to the bank. The note teller's department executes all commitments of this sort.

### Collection of Exchange Charges

The note teller's department also attends to the collection of exchange charges from those customers who desire to pay them in cash rather than have the bank charge their accounts for the amount. As has been indicated already, the transit department prepares bills for exchange and sends them to the customers. At the same time this department makes entry in the accounts receivable exchange book of the amount due from those customers who have indicated their desire to pay exchange over the window. This book is kept in the note teller's department. Customers then make payments of these bills to the note teller's department. The Exchange account of the bank is credited for the amount of the receipts from this source and the charges made against the customers are stamped out of the exchange book which is delivered to the note teller's department by the transit department.

### Receiving Operations

The department also acts as a receiving teller for certain special classes of deposits. The purpose of allocating this work to the note teller's department is to relieve the receiving teller of the special work which is required. Mention has already been made of the fact that the note teller's department receives items which are to be entered upon a collection, rather than upon a cash basis. Other transactions handled by the department for similar reasons consist of crediting accounts for incoming currency shipments and receiving country checks deposited by city correspondents, deposits requiring special advice and time deposits.

### Special Deposits

When a customer of the bank, an out-of-town correspondent, for example, sends currency by mail or by express for credit to his account, the shipment comes directly to the

paying teller On his daily proof the paying teller gives the note teller's department credit for the amount and sends the latter department a memorandum covering the details of the shipment The account is there credited according to the instructions of the sender Country checks from those city correspondents which use the transit department of the bank for collecting their out-of-town cash items are also received by the note teller's department This transaction arises from the reciprocal arrangement which the bank has with certain up-town correspondents These correspondents use the facilities of the bank to effect collection of their transit items and in return they collect items payable in their immediate vicinity for the bank

A more important class of deposits received by the note teller's department comprises those which require a special advice to be sent to some party other than the depositor Most numerous in this class are the deposits of branch offices of various concerns located in and about New York, particularly railroad companies Head offices of these concerns desire an independent check upon the cash of their branches They therefore have the bank send them, upon their special form letter, a daily report of the deposits which these branches have made during the day Besides these deposits which regularly require advices the note teller's department receives any other domestic deposit concerning which the bank is to send a special advice of credit

### Certificates of Deposit

Among the receiving operations of the department are those of receiving funds in exchange for which certificates of deposit, or deposit receipts, as they are commonly called abroad, are issued A certificate of deposit may be defined as an instrument evidencing a special deposit in a bank These deposits are special for several reasons They are not subject

to check and may be withdrawn only as a whole, not in part. Transfer of ownership of a deposit represented by a certificate may usually be made only on the books of the bank. The depositor may withdraw the amount deposited only after certain prescribed requirements have been met, such as after the expiration of a period of time, after a certain number of days' notice has been given, and the like.

### Classes of Certificates of Deposit

There are three kinds of certificates of deposit, the demand certificate, the definite time certificate, and the indefinite time certificate.

The demand certificate of deposit (Form 29) is a negotiable instrument made payable at the option of the beneficiary upon return of the certificate. It does not bear interest. The most common use of the instrument is that of transferring funds and for this purpose it has much the same advantage as the bank draft.

Time certificates of deposit are largely used for investment of idle funds. They bear interest at a rate agreed upon between banker and depositor. These instruments are non-negotiable, being assignable only on the books of the bank. Definite time certificates are drawn payable upon return of the certificate properly indorsed but after the expiration of a certain period of time, always 31 days or more. This stipulation is made for the reason that the Federal Reserve Act classifies deposits which are subject to withdrawal after 31 days as time deposits, and requires the debtor bank to maintain a lawful reserve of only 3 per cent against them as compared to one of 13 per cent against those payable upon shorter notice.

Indefinite time certificates (Form 30) are drawn payable upon a certain number of days' notice by the payee, but only after a certain minimum period of time has elapsed. While

*Certificate of Deposit*  
 No. 14399 April 5, 1921  
 \$6541.32  
 Deposited by  
Edward B. Loss  
 for Edmund Burke  
W. H. W. RB  
 55 Wall Street  
 The National City Bank of New York.  
 New York April 5, 1921  
Edward B. Loss has deposited in this Bank  
 six thousand five hundred thirty one  $\frac{32}{100}$  Dollars  
 payable to the order of Edmund Burke  
 member of this Certificate  
 \$6541  $\frac{32}{100}$  Robert Bagan Harold H. White

Form 29 Demand Certificate of Deposit (Size 11  $\frac{3}{4}$  x 3  $\frac{1}{2}$ )

*Certificate of Deposit*  
 No. B 10073 April 5, 1921  
 \$12,452.96  
 Deposited by  
Howard Jones  
 for Harold H. White  
 55 Wall Street  
 The National City Bank of New York.  
 New York April 5, 1921  
Howard Jones has deposited in this Bank  
 twelve thousand four hundred fifty two  $\frac{96}{100}$  Dollars  
 payable to the order of Harold H. White  
 member of this Certificate  
 \$12,452.96 Robert Bagan Harold H. White

Form 30 Indefinite Time Certificate of Deposit. (Size 11  $\frac{3}{4}$  x 3  $\frac{1}{2}$ )



such certificates are payable at the option of the holder after the minimum date for payment has arrived, the bank virtually fixes a maximum time during which the item is to remain outstanding by inserting a provision that interest upon the amount of the certificate shall cease after a certain date

Certificates of deposit are issued upon the application of the customer and with the approval of the officer of the bank. For each certificate the issuing clerk prepares two stubs, one of which is retained by the official signing the certificate and by him turned over to the auditors, while the other remains in the certificate book as a record of the transaction. The bookkeeping entry covering the issuance of a certificate of deposit consists of a debit either to cash or to the applicant's account, and a credit to Certificates of Deposit account.

### Telegraphic Transfers

The nature of telegraphic transfers may be illustrated by a typical transaction, although in actual practice there are almost endless variations from the types here shown. Suppose that A, a customer of the National City Bank of New York, desires to send \$10,000 quickly to his agent B in San Francisco. A would apply at the window of his bank for a telegraphic transfer tendering his check for \$10,000 in payment. His bank would then telegraph its correspondent in San Francisco to pay B \$10,000 and charge the amount to its account. The San Francisco bank would notify B upon receipt of the telegram and upon proper identification it would pay him the funds. The New York bank would credit the account of the San Francisco Bank for \$10,000 and the San Francisco bank would debit its account with the New York bank for a like amount. The transfer would thus be complete within a very few hours at the most and without the expense or delay of actual shipment of either cash or credit instruments.

In practice this typical transaction appears in a variety of forms. Instead of applying for the transfer in person at the window of the bank, the customer may write or telegraph, and instead of paying cash he may request the bank to charge the amount involved to his account. At the paying end of the transaction, likewise, some variations are to be noted. Instead of making actual payment to the transferee, the paying bank may credit his account as an ordinary deposit, or it may be called upon to send him a written or telegraphic letter of advice to the effect that the funds are being held subject to his orders. Quite frequently the paying bank is requested by its own customers to make deposit of funds with neighboring banks for use of the customers of these latter institutions.

### Outgoing Transfers

The transaction of handling telegraphic transfers may be described best by considering the transaction first from the standpoint of making the transfer, and second from that of making payments in accordance with the orders of out-of-town correspondents. An applicant for a telegraphic transfer is required to sign a regular application form at the window of the bank, or he sends a letter or telegram requesting that the transfer be made. The application contains the name of the applicant, the date, the place to which funds are to be sent, the name of the one who is to receive them, and special instructions as to advising the transferee, etc.

Upon receiving such an application the time of receipt is stamped upon it and the necessary charge and credit tickets, letters of advice, and telegrams are prepared. The bank mails an advice of the transaction to the sender and in case his account is to be charged this advice is prepared in duplicate, one copy of which is sent to the customer and the other to the bookkeepers of the bank to serve the purpose of a debit ticket carrying authority for charging the customer's account.

The bank also sends an advice to the one to whom funds are transferred. This latter advice, which is sent by mail, serves the purpose merely of confirming the transaction. An office copy of the telegram and a ticket crediting the account of the bank which is to make the payment are also prepared. All of the above tickets are made out with one operation as a device for saving time and effort.

Immediately after the receipt of the application for a telegraphic transfer the telegram embodying the details of the transaction is prepared in triplicate, is signed by an officer of the bank, and sent to the test word department for the test word, which serves the purpose of a signature on a telegram. The copies are then sent to the telegraph and cable department for transmission. This department despatches the telegram in code, stamps a copy of it with a time stamp, and returns it to the note teller's department. This copy is filed with the application of the customer as evidence that the transaction has been completed. The time stamps—one on the application, showing the time of receipt, and the other on the duplicate message, showing the time of transmission—serve the purpose of indicating the degree of expedition with which the work was handled.

The application of the customer frequently consists of a telegram instead of a letter. These telegrams come into the bank through the telegraph and cable department, they are passed to the test word department for verification and then to the note teller's department which has a "hold" placed by the bookkeepers of the bank against the account of the applicant and then completes the transfer in the regular way.

### **Payments under Telegraphic Transfers**

When the bank acts as paying agent under a telegraphic transfer the note teller's department receives the telegram from the correspondent through the channel indicated in the

preceding paragraph and makes payment to the beneficiary according to the tenor of the message. In general there are two methods of making such payments, in cash, and by crediting an account.

In the first place the bank may be asked to make payment over the window or by messenger to some individual or bank, including the federal reserve bank. The bank makes payment to the federal reserve bank by sending it a check drawn against its account with that institution, while it pays an individual or another bank within the city by sending a cashier's check, or by having the payee call at the bank and upon proper identification receive the funds. In recording payment made in funds, the Cashier's Check account, the Lawful Reserve with the Federal Reserve Bank of New York account or cash is credited, according to the method of payment employed. When cashier's checks are issued in payment of transfers, duplicate receipts are obtained from the recipient of the check, one copy is kept as a record, the other is sent to the customer who ordered the payment to be made. This copy serves as an advice to the customer showing that payment has been effected.

The second way by which the bank makes payment under a transfer is by means of a credit to the deposit account of the beneficiary. In recording a payment made in this way the note teller's department prepares a ticket crediting the customer's account. The beneficiary is sent an advice of the credit either by mail or by telegraph, according to the instructions of the incoming telegram. Office copies of all advices sent out are retained in the department for the use of the auditors in checking the telegraphic transfer operations.

#### Issuance of Cashier's Checks

One of the miscellaneous activities of the note teller's department consists of the issuance of cashier's checks. A

cashier's check is a check drawn by the bank upon itself. These checks are very extensively used by the bank in making direct payments to those to whom it becomes indebted. They are also used to a limited extent in place of certified checks and bank drafts in making transfers of funds from place to place.

In addition to issuing cashier's checks to customers who wish to use them to transfer funds, the note teller's department issues those which are required for making payments to beneficiaries under telegraphic transfers, to sellers of commercial paper, etc. Checks are also issued by this department for certain other departments in the domestic division of the bank. In a large bank it is impossible to centralize the issuance of cashier's checks in one department without impeding the progress of the work in the others. Hence such departments as the foreign teller's, the commercial credit, and the loan, which have many transactions each day calling for cashier's checks, issue their own checks. On the other hand there are departments, such as the bond, city collection, etc., which have only relatively infrequent need for cashier's checks. In the domestic division of the bank the note teller's department has the function of supplying such departments as these with their requirements.

Blank cashier's checks are numbered serially, the numbers being preceded by a key letter which indicates the department issuing them. A rigid control system is placed about the issuance of these checks. The clerk who prepares them is required to account for all numbers delivered to him. They are issued only on the authority of an officer of the bank who retains the stubs of the checks which he signs. These are sent finally to the auditors who use them to check the authority for issuance.

The accounting procedure for cashier's checks is as follows. At the time of preparing the checks duplicates of both

the check and its stub are prepared. The duplicates which accumulate in this way are sent to the general bookkeepers where they are filed by number. A credit ticket carrying a credit to the Cashier's Check account is also sent. As the cashier's checks come in for payment, the Cashier's Check account is debited and for verification the originals are compared with the duplicates on file, marked "Paid," and filed in a paid file for auditing.

### Issuance of Bank Drafts

A large New York bank has only occasional calls for bank drafts. The funds of this city, i.e., checks drawn upon New York, are desired by banks throughout the country who use them to build up balances in this city. Under such circumstances the personal checks of the customers of New York banks tend to be used to the exclusion of the bank drafts in making transfers of funds to points outside the city. Occasionally customers of the bank have need for bank drafts, however, and whenever they are to be issued the note teller's department attends to the work. Such a draft is illustrated in Form 31.

The bank draws either upon a correspondent or upon one of the federal reserve banks. Drafts of a face value of \$5,000 or less are drawn upon out-of-town correspondent banks unless federal reserve checks are specified in the customer's order, while those of more than \$5,000 are drawn, if possible, upon one of the federal reserve banks or branches. In drawing a bank draft upon a correspondent bank the drawer bank credits the account of the drawee bank and sends a letter of advice requesting that the draft be honored (Form 32). In drawing a draft upon an out-of-town federal reserve bank, the drawer bank advises both the drawee and the local federal reserve bank of its action. The former federal reserve bank is requested to charge the account of the latter instead

No C 2952	The National City Bank New York (NS)	
April 5 1921	New York	April 5 1921
Pay to Philip Lucke	Pay to the order of	Philip Lucke
Drawn on	Ten thousand dollars	no cents <del>xx</del>
1st - 2nd N.Y.	To First - Second National Bank	
Seattle, Wash	Seattle, Wash	Harold H. White Cashier
\$ 10,000 <del>xx</del>	No C 2952	
H.H.W.		

Form 31 Bank Draft upon Correspondent Bank (Size 11 x 3½)

of settling with the drawer bank direct since the New York bank maintains a reserve account only with the New York Federal Reserve Bank. The out-of-town federal reserve bank is also requested to advise the New York bank of its action.

The drawer bank credits its Lawful Reserve with the Federal Reserve Bank account. The local federal reserve bank charges the drawer's account and credits the paying bank, confirming the transaction by means of a notice to the drawer.

THE NATIONAL CITY BANK OF NEW YORK		
IN REPLYING REFER TO NOTE TELLER		New York, April 5, 1921
First-Second National Bank, - - -		
- - - Seattle, Washington - - -		
We have to-day drawn on you as follows		
No.	FAVOR OF	AMOUNT
0 2883	Philip Locke	\$10,000.00
Please honor upon presentation and charge to our account, returning the cancelled item to us. We have credited your account.		
Yours very truly		<i>James McKittrick</i> - - - Cashier

Form 32 Advice Requesting that Draft be Honored (Size 8½ x 5½)

The two federal reserve banks settle through the Gold Settlement Fund at Washington. By means of the workings of the Gold Settlement Fund, therefore, each member bank of the federal reserve system has facilities for drawing drafts not only upon the local federal reserve bank with which its lawful reserve is deposited, but also upon all other of the federal reserve banks and branches.

### Commercial Paper Purchases

Many out-of-town correspondents of the bank invest their surplus funds in commercial paper. The chief market for



this commodity is the open market of New York City. As a service for these correspondents, the New York bank attends to purchasing paper for them. Upon receipt of an order to purchase commercial paper the officers who purchase notes for the bank's own investments make the selection and agree upon terms with the broker. After having made the purchase, the officers send to the note teller's department a copy of the correspondent's instructions and a slip showing the terms. The broker from whom the purchase is made delivers the paper in accordance with the terms and receives in payment a cashier's check. The account of the correspondent is charged for the amount involved and the paper is either held for collection at maturity as a regular collection transaction or sent to the correspondent, according to his wishes.

### **Remittances Received Without Instructions**

It occasionally happens that a bank receives remittances which are not accompanied by instructions sufficiently clear to enable it to dispose of the funds. Remittances of this sort are sent by the various receiving departments to the note teller's department for adjustment. Pending adjustment such funds are credited to the Cashier's account of the bank, which account serves the function of holding funds which cannot be credited elsewhere. The note teller's department communicates with the remitter and follows his instructions in disposing of the remittance.

### **Returned Vouchers**

Occasionally an irregular check is passed by the check desk of the bank. Other clearing house banks also fail at times to detect irregular checks presented by the bank through the exchanges. Checks of this sort eventually find their way to those who drew them and the drawers upon detecting the irregularities return such items to their banks. Since the

New York bank is either the drawee or an indorser these items come to it for adjustment. The note teller's department receives items of this sort and issues receipts in exchange for them. The irregularities are then corrected and the corrected items delivered to those who hold the receipts.

### **Payment of Notes and Acceptances**

Sometimes the bank makes payment of notes and acceptances for those who do not have an account with it. Then, too, customers often desire to pay their notes which have been made payable at the bank in cash rather than have the bank charge them to their deposit accounts. Such clients send remittances for these purposes to the note teller's department. The Cashier's account is credited for the funds, and payment made upon the proper date and charged back to this account.

### **Disposition of Receipts**

The various cash items which the note teller's department receives during the day are of the same nature as those of the receiving teller's department. In addition to those received from its own operations this department acts as a sorting agent for other departments which do not receive a volume of work sufficient to make it economical for them to operate separate sorting forces. Such departments as the coupon collection, the loan, and the bond, charge their day's receipts to the note teller's department in bulk where the sorting force classifies them and charges them to the proper departments along with the items from the department's own work. These items consist of currency, sights, trusts, country items, and checks drawn upon the bank itself. They are charged and routed to the cash departments of the bank in the regular way. To care for the credits which arise in this department a credit journal is operated which is the same in principal and operation as that operated in the city collection department.

## Departmental Daily Proof

The daily proof of the note teller's department (Form 33) does not differ essentially from that of other departments of the bank. It consists of a record of cash items coming into the department on the one side and the disposition of

THIRD TELLER'S PROOF, <u>Dec 31</u> 1921					
Transit Dept	14, 703, 379 55	Journal,	48, 805, 536 53		
Check Clerk (8 s)	21, 402, 894 32				
1st Teller,	19, 623, 165 34	1st Teller,	14 73		
" " (Hold over)	10, 361 05	2nd "	41 83		
2nd "		4th "	7 67		
4th "	219, 498 31	5th "			
5th "		Bond Debit	75, 053 36		
" " (Small Coins)	486, 703 56	Broken Colln	69, 294 23		
" " (Trust Co's)	755, 617 32	Check Desk	587, 410 86		
" " (Sight Drafts)	2, 451, 530 77	Discount Debit	9, 282, 600 94		
Clearing House Exchanges,	14, 100, 264 23	Loan Debit	14, 883, 438 70		
		Accounting Debit	50, 015 60		
Total	73, 753, 414 45	Total	73, 753, 414 45		

Form 33. Note Teller's Daily Proof (Size 7½ x 8½)

those items to the various tellers and departments of the bank on the other.

## Collection of Coupons

In New York City the work of collecting coupons and bonds which have fallen due or have been called for payment is particularly heavy. Most of the large borrowing corpora-

tions and municipalities have their financial offices in New York or they maintain paying agencies in this center for paying their obligations. Out-of-town banks and other customers send coupons from their holdings and from those of their customers to their New York City correspondent for collection and credit. Local customers add to the volume of the work by sending their maturing bonds and coupons to the bank for the same purpose. Matured bonds and those which have been called for payment by the debtor concerns are forwarded along with the coupons. The New York bank therefore becomes a collection agency for items of this sort from every part of the country. In addition to those collections which are sent into the bank by mail and over the note teller's window upon a collection basis, the work of collecting coupons is augmented by material from other sources. In the first place the bank maintains a regular service which consists of holding bonds in safe-keeping for its customers and attending to collecting the income and the principal of these bonds as they mature. In the second place bonds are very often held by the loan department of the bank as collateral against loans which have been granted to customers. If the customer desires the bank to do so the income from such securities is collected for him. In the third place coupon collections arise from the bonds which are held by the bank itself as investments, and from those held in connection with trusts of the trust department. Because of the extreme heaviness of this work of collecting coupons and of the specialized service which must be performed in connection therewith, a department known as the coupon collection department specializes upon collections of this sort.

The work of the coupon collection department is quite similar to that of the city collection department. The items are entered in a similar collection register which, however, is kept in the registered mail department of the bank in

order to provide a control over the items flowing into the coupon collection department from all sources. The coupon collection department covers the same territory as the city collection department, it likewise collects by messenger, it receives the same class of funds, and it makes payments to customers in the same way as does the city collection department. Owing to the above-mentioned similarities only the distinctive features in collecting coupons need be mentioned.

### **Ownership Certificates**

All coupons other than those detached from obligations of the United States or any of its political subdivisions must be accompanied by a certificate of ownership made out on one of the forms prescribed by the Treasury Department. The purpose of these ownership certificates is to guide the paying agent in accounting for the income tax which is to be paid at the source and to enable the Collector of Internal Revenue at Washington to check income tax returns filed by taxpayers. These certificates are of three classes: one class for owners of certificates who claim exemption from the tax, one class for those who do not claim exemption, and one class for those who are collecting the income from foreign securities.

### **Unmatured Coupons**

Often coupons which have not yet matured are received. In cases of this sort the customer is communicated with to ascertain whether he has sent unmaturing coupons in error, and after it has been definitely established that the customer desires such action, these items are held for collection at maturity much as unmaturing notes and acceptances.

### **Coupon Envelopes**

Incoming coupons are received in envelopes which take more or less of a standard form, as shown in Form 34.

The envelope contains on its face some such information as the name of the sender, amount of coupons, issue concerned, and the maturity date. As these envelopes pass from bank to bank and from agent to agent they are indorsed on the back with the regular bank indorsement stamp in the same way as are checks, drafts, and other negotiable instruments. When one of these envelopes is received a serial identification or collection number is stamped on the envelope and each item of the contents, both coupons and ownership certificates. The contents of the envelope are then carefully

Name <u>Henry S. Brown</u>	
Address <u>905 West End Avenue</u>	
City and State <u>New York</u>	
Coll. No. <u>      </u>	Letter Date <u>Dec. 23 1920</u>
Kind of Coupons <u>Chicago, Rock Island &amp; Pacific R.R.</u>	
<u>11</u>	Coupons ea. \$ <u>20</u> \$ <u>220<sup>00</sup></u>
<u>      </u>	" " \$ <u>      </u> \$ <u>      </u>
Due <u>Jan. 1, 1921</u>	Total <u>220<sup>00</sup></u>

Form 34 Coupon Envelope (Size  $5\frac{1}{2} \times 3$ )

counted and verified and on the outside of the envelope is indicated the name of the local paying agent to whom presentment is to be made. Coupons which are payable out of town are sent to the country collection department if they are domestic coupons or to the foreign collection export department if they are foreign coupons and these departments effect collection. They pay the proceeds to the coupon collection department and it settles with the customers in the usual way.

### Payment of Coupons

The majority of the paying agents require that coupons which are being presented to them for collection be enclosed in envelopes of their own special design. Such an envelope is shown in Form 35. The coupons are assembled according to issue and are enclosed in the required envelopes, and those envelopes which are to be presented to each paying agent or at each messenger's "stop," as the places where presentations are to be made are termed, are enclosed in a larger envelope. This envelope gives on the outside a list of its contents and the totals on these envelopes prove with a route sheet which has been prepared for the messengers. As the messengers return the coupon checks received in payment of their collections together with the unpaid items they are checked against the route sheets. The department forwards the cash items it has received to the note teller to be handled in his cash rack. In the meantime credit tickets and letters of advice have been prepared and these are passed through the credit journal of the department. The credit tickets are then sent to the bookkeepers and letters of advice of collection to the owners of the item.

### Unpaid Coupons

Coupons are quite commonly returned unpaid because the paying agent has not received funds from which to make the payment, because stop-payment orders are in effect against them, because they are not due, have been sent to the wrong paying agent, or because the ownership certificate is not properly executed. Unpaid coupons are handled in the same way as the unpaid items of the city collection department except that they are not protested. Most generally the irregularity which prevents immediate payment from being made is corrected in the course of time and the collection is completed without returning the coupon to the owner.





### Coupon Collection Department Proof

The proof of the day's work in the coupon collection department is prepared on the form shown in Form 36

### Collection of Country Items

For the collection of non-cash items payable out of town, a country collection department is in operation. This department has the same relation to the collection work of the bank as the transit department has to the cash work. Thus the country collection work includes items of the same class as appear in the collection work of the city collection, note teller's, and coupon collection departments, but payable outside the city. In addition the maturing discounts payable out of town are collected through this department.

The method used by the bank to collect its country collection items is practically the same as that which it uses to collect the transit items. Arrangements are in effect to collect each class of items either through a correspondent bank or one of the federal reserve banks. Comparatively few are collected through the federal reserve banks, the most frequent class being bankers' acceptances. When items are to be collected through the federal reserve banks direct sendings to out-of-town federal reserve banks and branches are not made. Collection items can usually be despatched long enough before they are due to reach the drawees or makers on the date of maturity, and they are therefore sent through the Federal Reserve Bank of New York.

In the country collection work, whether effected through the federal reserve banks or through correspondents, there is this one important difference between the work of handling collection items and that of handling cash items. Cash items are generally charged to the account of the collecting agent to which they are sent without specific acknowledgment from that agent that collection has been effected. Collection items



on the other hand are sent to collecting agents with the understanding that they are to make settlement only after actual collection has been effected. Charge is therefore made in most cases only after advice of payment has actually been

HELD OVER FOR TOMORROW		
19 307 94	New	
53 797 76	In Box	
14 976 60	Holding a/c Certificates	
39 282 38	Outstanding Country Items	
134 631 52	" F X "	
12 545 10	Odd	
	Liberty Loan Cash	
85 09	" " Route	
	" " "	
	" " "	
	" " "	
89 731 56	Route	
146 055 23	3/1 2nd route	
58 985 39	3/1 return	
174 562 93	4 To holding	
743 957 50	TOTAL	

Form 36. (b) Coupon Collection Department's Daily Proof (reverse)

received. In other words, in collecting cash items the bank assumes that collection has been successfully made unless it has specific information to the contrary, while in handling collection items it makes settlement with the client only on the authority of definite knowledge that collection has been effected by the correspondent.

### Collection Number and Stamp for Country Items

To each incoming item, excepting foreign ones, is assigned a serial collection number. This number is placed upon the face of the item by means of a stamp of distinctive shape and the item is described and referred to by this number as it progresses through the collection work. In case it becomes necessary for the out-of-town collecting agents to return country collections unpaid, this stamp enables the clerks of the mail teller's department to recognize the incoming items as collection returns and to forward them promptly to the country collection department.

### Record Files

With each country collection item comes the customer's letter of instructions. These letters are used in preparing quintuplicate record and bookkeeping tickets after which they are returned to the mail teller for acknowledgment. On the tickets prepared by the country collection department is recorded such information as the date, the owner's name and address, maker's name, drawee's name and address, where payable, date sent, due date, date of owner's letter, owner's number, the bank's collection number, amount, and instructions as to protest, wire fate, etc.

One copy of the ticket serves as a letter of transmittal (Form 37) which is sent to the out-of-town correspondent along with the item to be collected. In case items to be collected consist of those payable to bearer, such as coupons, the remittance is enclosed in a special envelope which is prepared concurrently with the tickets and the letter is sent by insured registered mail. With each letter is enclosed a postal card which is to be returned by the correspondent immediately after receipt of the letter as an acknowledgment of safe arrival.

A second copy of the ticket is retained as a record of the transaction. Tickets representing outstanding collections

for which advices of fate have not been received are filed separately from those for which such advice has been received. By means of this method of filing, the outstanding collections may be quickly examined and those which have been outstanding for an unreasonable period of time are brought to attention and followed up.

The National City Bank of New York,			
Union Trust Co. Chicago Ill.		April 28, 1921	
For Collection and Advice of Payment.		Do Not Credit Until Paid.	
Please Advise by Number			
<small>UNLESS OTHERWISE INSTRUCTED Do not hold collections for the convenience of parties. Surrender documents attached to drafts only on payment of value. PROTEST and RETURN without delay all dishonored paper. Wire all unpaid or unaccepted items over \$500.</small>			
No enclose for collection		DO NOT PROTEST ITEMS \$10.00 OR UNDER	
Our Number	DRAWEE	INSTRUCTIONS	AMOUNT
65829	J. R. Moore & Co	Documents to be delivered on acceptance	327.40
65830	J. R. Williams & Son	60 day Draft for acceptance and return	2,140.35
65831	White & Jones	Wire-Date	3,104.06

DO NOT PROTEST ITEMS BEARING THE SYMBOL..(N.P.18)

Form 37 Remittance Letter for Collection Items (Size 8 x 7)

A third copy of the ticket serves as an advice of payment to the owner. These are filed in the department and when an item has been collected the corresponding ticket is sent to the owner as advice of payment.

#### Settlement for Items Collected

As has already been stated, the bank makes settlement only after advice of the completed transaction has been re-

ceived from the out-of-town collecting bank. Two settlements are to be effected. One consists of recovering from the collecting bank, and the other of paying the owner. Entries to record these settlements are made by "putting through" copies of the tickets which were prepared and filed when the collections were entered. One copy of each ticket serves as a debit ticket covering settlement with the correspondent which made the collection, and another serves as a credit ticket covering settlement with the owner.

In case the federal reserve bank has made a collection it sends an advice stating that collection has been effected and that the account of the New York bank has been credited for the proceeds. Settlement with the federal reserve bank is made therefore by passing the debit ticket covering the amount involved to the account Lawful Reserve with the Federal Reserve Bank of New York.

In the case of items which the bank has sent to correspondents other than the federal reserve bank, these banks send advices that collections have been made and they settle with the New York bank by requesting that their accounts be charged or by enclosing a remittance. If the first method of settlement is to be used the debit ticket is sent to the bookkeepers for posting to the debit of the correspondent's account. If, on the other hand, the correspondent is to send a remittance, the debit ticket is passed to the collection ledgers to be debited to the correspondent's special account contained in these books. The mail teller sends the remittance letter which he receives from the correspondent to the collection ledgers for credit, and thus the country collection department's charge is offset by the credit arising from the remittance.

The bank settles with the customer according to his instructions. In case he has requested the proceeds to be placed to his credit, tickets crediting his account are sent to the bookkeepers and an advice of credit is mailed to him. In case

the customer desires a remittance, however, the Cashier's Check account is credited and the cashier's check is sent to him in the usual way. As in the case in all collection transactions made by the domestic departments for the foreign collection import department, completed transactions of this sort are

THE NATIONAL CITY BANK OF NEW YORK					
				New York, April 30 _____ 1921	
Dear Sirs—					
Kindly note that our correspondents advise that they are holding, unpaid items which we received from you for collection as indicated below. Please instruct us definitely as to their disposition in the columns provided and return this form to us at your earliest convenience.					
Date of Your Letter	DESCRIPTION	AMOUNT		Reason for Non-Payment	Disposition as to Disposition
4/27	White & Jones, Chic.	\$	104 08	Drawers claim goods are not as represented	

NOTE—(We are entirely dependent upon the statements of our correspondents for information regarding such collections and must be guided by your instructions in disposing of the above items)

To J. B. Wilson & Son Yours very truly  
New York COUNTRY COLLECTION DEPT

*W. A. P. White*

(The customer receiving this blank should fill it out and return it as promptly as possible to THE NATIONAL CITY BANK OF NEW YORK.)

Form 38 Advice to Owner of Non-Payment of a Collection Item (Size 8¼ x 5½)

reported to that department upon the regular duplicate ticket and that department makes settlement with the owner

### Collection of Discounts and Bankers' Acceptances

Exceptions to the method of settling with correspondents by charging their accounts are made in the cases of items from the discounts of the bank and of bankers' acceptances. These are made payable either by or at a bank and they are charged to the accounts of collecting agents upon maturity dates without waiting for letters of advice of payment from such agents.

### Collection Charges

Exchange charges are collected upon the majority of the country items collected. This difference from the practice in collecting city items arises from the fact that by the rules of the New York Clearing House Association items drawn payable in the city of New York are classed as "discretionary" with member banks in assessing exchange charges, while country items are not usually so designated.

Pursuing the idea of service, the bank as a general rule charges its clients the minimum exchange rate of the clearing house provision rather than the larger one which it would be permitted to charge. The collection charge is credited to the Exchange account and deducted from the proceeds of the collection.

### Unpaid Country Collections

Unpaid items come to the mail teller and they are returned to the country collection department after protest fees have been taken care of by the city collection department. The country collection department then returns each item to the last indorser, together with an advice (Form 38) giving the reason for non-payment.



## CHAPTER VIII

### FOREIGN COLLECTIONS

#### Nature and Scope

Before discussing the foreign collection activities of a bank it is advisable to consider briefly the various items which enter into or make up the material of this work, together with the various transactions which give rise to them. The term "foreign collections" as used in its banking sense includes two classes of items: (1) those payable abroad, and (2) those payable in this country which are received for the account of foreign customers of the bank. The former class may be termed "outgoing," or export, collections, while the latter may be termed "incoming," or import, collections.

The terms "export" and "import" as they are used here must not be confused with exports and imports of merchandise. It is true that the large bulk of the export collections arise from exports of merchandise from the United States, and likewise the import collection items are in many cases closely related to importations of goods. The terms "export" and "import" collections, however, refer to the directions in which the items themselves are headed through the collection process rather than to their source. Export collections are outgoing to foreign countries, while import collections are incoming from abroad.

#### Origin of Foreign Items

The specific items which enter into foreign banking business consist almost exclusively of drafts or bills of exchange, but there are also such instruments as checks, money orders, coupons, called and due bonds, coupon checks, certificates of

deposit, drafts upon savings banks accompanied by savings bank books, travelers' checks, etc. These items come from various sources. In general, however, they may be divided into five main groups:

- 1 Foreign trade
- 2 Insurance, freight, etc
- 3 Foreign investments (purchase and sale of securities and maturity of coupons and securities)
- 4 Bankers' loans to each other
- 5 Remittances made by immigrants to persons in the home country, expenses of travelers, etc.

Of these sources, the foreign trade contributes the great majority of the collection items

### Settlement of Foreign Debts

One use of the draft in foreign business which gives rise to a large amount of foreign collection work for the bank is that of settling accounts and of transferring funds. The nearest resemblance to this type of foreign draft is to be found in the domestic dunning draft. It should be observed at this point that none of the odium is attached to a foreign draft when issued to effect the collection of an account that is attached to the domestic draft, in fact this method of collection is quite the approved form in foreign business. If a creditor in the United States desires to collect a bill from a foreign debtor, for example, the most usual method of settlement is for the creditor to draw a draft upon his foreign debtor. Such a draft is then entered with the drawer's bank for collection, or for acceptance and collection, and it becomes a part of the material upon which the foreign collection department works.

A similar use of the foreign draft occurs in cases where one concern wishes to remit money to another. Foreign con-

cerns, such as insurance companies desiring to remit to their branch offices or to others in the United States, quite commonly have the local concern which is to receive funds draw a draft upon them for the amount in question. This draft is then entered with the American bank for collection.

### C. O. D. Transaction

A second use of the foreign draft which brings the collecting activities of the bank into action is that of shipping goods to a foreign country on a collect-on-delivery basis. This transaction is identical with the domestic transaction, which consists in shipping merchandise under an order bill of lading attached to a draft. One of the most common methods of financing foreign trade is by means of the draft with documents attached. In a transaction of this sort the shipper of the merchandise loads his goods, prepares the proper documents representing title to them, attaches the documents to a draft drawn upon his foreign customer, and instructs his bank to effect collection, making delivery of the documents to the foreign customer upon payment or upon acceptance of the draft. By this means of financing, the seller retains a lien upon his shipment, assuring himself that he will receive payment before the merchandise goes out of the possession of his agent, the bank. The purchaser of the goods, on the other hand, pays for them only as they come into his possession. In addition to covering the sale of goods, drafts of this sort may be used in connection with stocks, bonds, and other valuable papers for delivery against payment in much the same way as domestic stock drafts.

### Duplicate Items

The foreign draft boasts of a lineage dating back to the Middle Ages. In an age when the uncertainties of transportation were augmented by many risks which have long since been

overcome, the custom of drawing important documents in several copies was devised as the only practical means of insuring safe delivery. The Venetian merchant, it is said, drew his bill of exchange in several copies putting each in the hands of the master of a different ship for delivery. The first copy to arrive at its destination was honored. If perchance a second or a third copy arrived it was by common understanding void. This custom is still followed in foreign financing. Importers, exporters, banks, and other concerns transacting international business, draw their various documents at least in duplicate and forward each copy by a different mail steamer. The first copy arriving at destination becomes the valid copy, thereby voiding all others. In this age of safe transportation the chief function of the duplicate is, of course, that of eliminating delays, rather than insuring ultimate safe delivery.

### **Tenor and Usance of Drafts**

As to tenor, there are two classes of drafts (1) the sight, or demand, and (2) the time draft. These two terms have the same meaning in foreign banking as in domestic. The time draft is divided into two subclasses viz., short bills and long bills. A short bill is one drawn for 30 days or less, while a long bill is drawn for more than 30 days, usually up to 120 days. As to usance, time drafts are of two classes: those which are drawn payable a certain number of days after date, and those which are drawn payable a certain number of days after sight or acceptance.

### **Clean and Documentary Drafts**

Foreign drafts may be divided further into classes according as they are, or are not, accompanied by documents. A draft which is accompanied by documents is termed a "documentary" draft, while one which is not so accompanied is termed a "clean" draft. The term "documents" may be used

to designate any valuable papers attached to drafts, such as shipping documents, securities, insurance policies, etc., but in practice the term generally refers to shipping documents. Even in this usual case, however, the term is rather variable in meaning, or rather the specific documents which are included may vary somewhat from transaction to transaction. A description of some of the principal instruments included in the term "documents" follows.

### **Ocean Bills of Lading**

The ocean bill of lading is the essential document in connection with a foreign shipment. This document, like the domestic bill of lading, is both a receipt for goods delivered to the transportation company by a shipper and a contract between the transportation company and the shipper covering the conditions under which the shipment of the goods is to be made.

An ocean bill of lading is drawn up in several copies, depending upon the circumstances. Some of the copies are negotiable and others are not. The negotiable copies represent title to the goods and are issued for the purpose of transferring them from one party to another, while the non-negotiable copies are used for purposes of record according to the needs of the shipper, the steamship company, the customs authorities, and the foreign buyer. The collecting bank is, of course, concerned only with the negotiable copies.

The full and complete number of negotiable bills of lading is termed a "set." There are generally three copies to a set. Possession of any one of these copies constitutes title to the goods, hence the bank makes sure that the complete set comes into its possession. The number of copies constituting a set may always be determined by consulting any one copy of the bill of lading, as each copy states the number which have been issued.

### Order Bills of Lading

Ocean bills of lading are drawn either to order or directly to the consignee. The order bill of lading is drawn to the order of the shipper or in blank and it is indorsed by the shipper to his bank, by the bank to its foreign correspondent, and by the foreign correspondent to the consignee of the goods, with the intention of passing title to the shipment or of holding a lien against it as the transaction proceeds.

Order bills of lading often have stamped on their margins what is termed the "notify" clause. This clause requests the transportation company to notify the designated consignee when the goods arrive at destination. The purpose of the notification clause is not to give the consignee any claim upon the goods, but to enable him to make financial and other arrangements for promptly taking possession of the shipment upon arrival.

The laws of certain countries prohibit the use of order bills of lading, and those of others do not provide for absolute protection to the shipper. Except where the laws of the country of destination forbid such bills to be drawn, shippers generally use order bills of lading in all cases where title to the goods must of necessity remain with the shipper or his collecting agent until collection has been effected. Whenever the laws of a foreign country do not place the same significance upon an order bill of lading as in the case of American law, those who are experienced in foreign trade consider that the order bill at least serves a valuable function as a moral weapon against the consignee's acquirement of goods before payment has been made.

### Marine Insurance Policy

Next to the ocean bill of lading, the marine insurance policy is probably the most important and the most common item included in the term "documents." Insurance covering

the various risks to which a foreign shipment is subjected is well-nigh universal. In contrast with the domestic railroad company which is by law virtually the insurer of the goods it carries, the ocean carrier is legally liable for only a very few of the risks of transportation. To protect the owner of the goods from these risks, marine insurance is generally written to cover each shipment, and the policy, or "certificate of insurance," as it is often termed, becomes one of the documents which strengthens the security of the instrument it accompanies.

### Miscellaneous Documents

Other items which may be included in the term "documents" are invoices, certificates of weight, analysis, inspection, origin, etc., consular invoices; non-dumping certificates, etc. The term "invoice" is used in foreign trade in the same sense as in domestic. The foreign invoice includes an enumeration of the goods contained in the shipment together with the selling price and also a statement of whatever charges, such as freight, insurance, exchange, etc., are included in the seller's total bill against the purchaser. Regarding such charges as insurance premium, ocean freight, etc., it should be remarked that they may be borne by the seller or by the buyer according to the terms of sale agreed upon. It is usual, however, for the purchaser to pay those expenses which occur in connection with the shipment after it has been put aboard ship by the exporter. Regardless of the tenor which the draft embodying the cost of the goods may take, such charges as these are often covered by a sight draft which accompanies the draft drawn against the goods themselves.

Certificates of weight, analysis, inspection, etc., are required by the customs authorities or by specific contract between the seller and buyer in the case of certain commodities. A consular invoice is a document certified to by a consul of the

country of the destination of the shipment, giving a description of the goods and a declaration of their value for the assistance of the foreign customs authorities. Certificates of origin certify that the merchandise covered by a shipment is a product of the country whence it is being exported. They are issued to obtain tariff preference in making shipments to countries with which "Most Favored Nation" treaty clauses are in effect.

Non-dumping certificates are for the purpose of showing that the exporter's price to the foreign buyer is not essentially lower than his price to buyers of a similar class in his own country. These certificates are required before goods can pass the customs authorities of certain countries, notably the British Colonies of Canada, Australia, New Zealand, and South Africa, which have laws against the dumping of goods in their markets by foreign sellers. The miscellaneous documents, including certificates of weight, analysis, inspection, consular invoices, certificates of origin, non-dumping certificates, and others, appear in a set of shipping documents according as the contract between buyer and seller, the nature of the commodity shipped, or the laws and customs regulations of the two countries demand.

The connection which exists between drafts and the accompanying documents varies with the agreement in effect between drawer and drawee. One of two conditions is generally prescribed by the drawer for the release of documents. They are to be released either upon acceptance or upon payment.

### **Bases of Handling Foreign Items**

The bank handles foreign items of the classes just enumerated on two different bases viz, the collection basis, and the discount basis. In foreign banking the operation of handling an item on a collection basis carries with it exactly



the same meaning as that of handling collection business in the domestic field. The bank acts as the agent of its customer in effecting collection, and after collection has actually been made it places the proceeds at his disposal. In handling items on a discount basis the bank virtually purchases the foreign item from its owner. The customer is given a part or the whole of the face amount of the item, less interest for the time which will be required by the bank in order to collect it.

### **Economic Aspects of the Foreign Collection Service**

The foreign collection service brings one or more of three economic services of the bank into action. In the first place the bank bridges the distance between the foreign and the domestic business man by placing local funds at the disposal of the creditor in exchange for distant ones. In the second place it performs the function of converting foreign money into that of the United States, or vice versa. A large number of the items handled in the foreign collection service are drawn in the currency of the United States and the mere collection of such items does not involve the changing of monetary units. In all cases, however, before the transaction is completely closed as between all parties concerned, the act of making a foreign collection will have involved the changing of the monetary units of one country into those of another. In the third place the bank performs the economic function of facilitating exchanges by bringing expert knowledge to bear in making adjustments of differences in national laws and customs.

### **Volume of Foreign Collection Business**

The foreign collection service is particularly large in volume and in importance in the case of a bank having numerous domestic and foreign correspondents. Interior banks,

even those of large size, do not generally find it profitable to maintain foreign correspondents. They accordingly accumulate the foreign business of their communities and pass it on to their New York correspondent. In addition certain large, non-banking concerns outside of New York City, mainly exporters and importers, find it worth their while to use the collection facilities of a New York bank in a direct way. There are also a large number of importers and exporters located in New York whose foreign banking business is transacted through their local bank. These various domestic concerns pour a great mass of collection business into the New York bank.

Abroad, the source of collection items is in most respects the same as it is in this country. Many traders located abroad maintain accounts with the New York bank or one of its branches and they receive the use of the facilities of the bank for collecting items payable in the United States through its city collection department, its coupon collection department, its clearing house connections, its transit department, and its country collection department as a part of its service to them. In addition to these customers which are not banks, the foreign correspondents and branches of the bank send their accumulations of items payable in the United States to New York for collection.

These two sources of collections give rise to the two classes of items mentioned at the beginning of the chapter—the export, or outgoing, class which consists of items to be collected in foreign countries, and the import, or incoming, class which consists of items coming from abroad for collection which are payable in the United States. To take care of these two classes of items, two departments are in operation in the bank. For the former there is the foreign collection export department, and for the latter, the foreign collection import department.

## EXPORT COLLECTIONS

### Items Payable Abroad

The work of effecting export collections may be conveniently divided into two parts first, the receipt, entry, and forwarding of the item for collection, and second, the payment or settlement with the customer for the proceeds after collection has been made. Items are received both over the window and through the mail. They may originate in the United States or in a foreign country, since the essential characteristic of the foreign collection export item is merely that it shall be payable in some foreign country.

### Receipt and Examination of Items

An item, consisting typically of a letter of instructions accompanied by a draft with documents attached, first comes to the attention of the receiving clerks who check the constituent parts against the letter of instructions from the owner. Important instructions contained in the letter are underlined in color to reduce the possibility of their being overlooked. Documents are carefully examined for indorsement, signature, and general form. After the items have all been examined a collection number is assigned to the transaction. Each item, including the letter, copies of the draft, documents, etc., is stamped with this collection number in order that any lost or misplaced items may be quickly identified if recovered. Distinctive numbers are used for collections so that they may be readily distinguished from discounts of the foreign discount department when advices come from abroad.

Items are often entered for collection on the day of departure of a vessel for the country of the drawee. The receiving clerk of the department keeps a careful list furnished by the outgoing mail department showing the sailing dates of the

various steamers leaving the port of New York, and collections requiring such action are marked specially with the name of the ship and rushed through the work in order that they may be forwarded in the proper mail.

### **Export Collections Register**

After letters of instruction have been noted and drafts and documents examined in a preliminary way, they are entered in a collection register which serves the function of recording the circumstances of the transaction for guidance in handling the item, in the same manner as the collection registers which are used in the domestic work of the bank. This register contains space for the following information: from whom received, for whose account, customer's collection number, date entered for collection, bank's collection number, drawee, to what foreign correspondent or branch sent for collection, amount, tenor, and disposition. Entry is made in the proper columns as the item progresses through the different stages of the collection process.

### **Tickets**

After collections have been entered in the collection register quadruplicate tickets (Form 39) which are to serve as charge and credit tickets and letters of advice are prepared. These tickets contain the following information: collection number given to the item by the bank, from whom the item was received, by whom drawn, his address, where payable, the amount, tenor, whether or not the item is to be protested for non-payment or non-acceptance, and whether the documents, if any, are to be delivered against payment or against acceptance.

The first copy of this ticket serves as a charge ticket, the purpose of which is to debit the account of the foreign bank after it has advised that collection has been made and that

the proceeds are to be charged to its account After it is determined to what foreign bank the item is to be sent for collection, the name of that bank together with a list of the

<b>THE NATIONAL CITY BANK OF NEW YORK</b> Foreign Office		In reply kindly refer to Our No F C <u>99999E</u>	
Acknowledgment of receipt only to be mailed to		New York <u>Jan. 6, 1921</u>	
Drawn by <u>Consolidated Tape Co.</u>		<u>Same</u>	
<u>149 South Street, New York.</u>			
We wish to acknowledge receipt of your draft drawn on <u>Bogota, Colombia</u> against <u>Delvalle Hermanos</u>			
Sent us in your letter of <u>Jan. 5, 1921</u> , your No <u>7853</u>			
Amount of draft <u>\$500.00</u>			
Tenor <u>120d</u> date <u>1/5/21</u>		with instructions { _____ to be protested for non acceptance _____ to be protested for non-payment	
Documents attached to be delivered against <u>acceptance</u>			
which we have entered for collection and will be pleased to account to you for the proceeds in due course Foreign Collection Dept Export			
SEE OTHER SIDE		<i>J. R. White</i>	

Form 39 (a) Ticket Acknowledging Receipt of an Export Collection (face).  
(Size 6 x 4)

<p>Please read this advice carefully, if not correct notify us at once</p> <p>Always give our number when communicating with us in connection with this item</p> <p>In connection with this collection we will exercise care in the selection of responsible correspondents and sub-agents as in the course of our own business, but shall not be liable for any neglect or default of any correspondent or sub-agent so selected or for any loss of such paper or its proceeds during transmission</p>
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Form 39 (b) Ticket Acknowledging Receipt of an Export Collection  
(reverse)

documents making up the item is entered in ink on this copy of the ticket If the collection item has been sent to the foreign bank on a remittance basis, this charge ticket charges the Collection rather than the Deposit account of the collecting bank

The second copy of the ticket is for the purpose of crediting the account of the owner of the item or the Cashier's Check account, as the transaction may require, when settlement is made. The third copy is to serve as an advice of payment to the owner of the item. (See Form 41.) These three tickets are held in the files until collection is effected.

The fourth copy of the ticket serves as an advice that the collection has been entered, and is mailed to the customer on the day following entry. The bank thus gives the customer its version of the transaction and enables him to correct any errors which may have been made and to notify it, in most cases, in time for errors to be corrected by cable before the item arrives at the foreign bank for collection.

After these tickets and the advice have been prepared, each negotiable item is indorsed. In transacting foreign business a stamp is not sufficient to serve as an indorsement, the indorsement must be autographically signed either by a "per procuration signer," or by an officer of the bank. A per procuration signer (abbreviated P. P.) is one who has been given formal authority to sign for the bank. The signatures of all officers and per procuration signers together with a copy of the resolutions of the board of directors of the bank authorizing such signatures are on file with foreign correspondents of the bank.

The foreign correspondent or branch to which an item is to be sent for collection is chosen at this time. At this point it may be said that foreign collections are sent to correspondent banks and to branches in the same manner as domestic transit and collection items are sent to domestic correspondents. Items are sent to branches of the bank wherever possible and in other cases the business is distributed among the available correspondents in a predetermined ratio.

A record of the amount of business which is sent to each correspondent is kept. At the close of each day this record

is checked against cards showing the ratio in which the outgoing collection business is to be divided and deficiencies are noted. In sending out the next day's collections adjustments are made by sending the larger volume of collections to those banks which are short in their quotas.

Every care is taken to determine that all of the instructions of the customer have been noted and adhered to. Accordingly the tickets together with the customer's letter and the items accompanying it are taken charge of by a checker who very carefully compares the tickets with the instructions contained in the customer's letter.

### Letters of Transmittal

Items to be sent abroad for collection are enclosed with a letter of transmittal which serves the usual function of transmitting the items for collection and of giving the foreign bank instructions as to how they are to be handled. Three copies are written, the original and the duplicate are to be sent to the collecting agent, and the triplicate is to remain in the bank's files. These letters give the bank's collection number, the amount, the name and address of the drawee, whether the item is to be protested, the tenor, documents attached, and any special instructions of the owner, such as cable payment, "in case of need refer to       " etc.

At this point a second checking of the client's letter, the items, the tickets, and the letter of transmittal is made. At the same time any special instructions which pertain to the collection arrangement between the bank and its foreign collecting agent are stamped on the letter of transmittal. This final check, coming as it does after a close comparison of the tickets with the customer's letter, practically insures that the transaction will have been handled according to the desires of the customer and in keeping with the best arrangements prevailing with the available foreign collecting agents.

### **Forwarding Items to Collecting Agent**

The collection items are now ready to be forwarded to the foreign collecting agent. Duplicates of the letters of transmittal, drafts, documents, etc., are separated from the originals and sent to the outgoing mail department, which encloses each copy in a separate envelope and mails it. The envelope containing the originals goes forward by one steamer, while the envelope containing the duplicates goes forward by a second one in order that the loss or delay of one set may not hinder the transaction from being consummated.

### **The Ticket Files**

The various tickets are filed to await the time when collection shall have been effected. The credit tickets and the advice tickets are filed in separate compartments by names of the owners of the items. These files serve the purpose of indicating the amount of business which is pending for each customer and the approximate time when funds will become available for credit to his account. The debit tickets are filed according to the location of the bank which is to be charged. After this filing the work of handling the transaction has been completed, so far as the bank at this end of the transaction is concerned, until such time as settlement for the collection is in order or a follow-up on the item must be made, owing to a delay in payment. An exception to the foregoing statement is to be noted, however, in case the owner of the collection desires to change his instructions.

### **Advices of Receipt and Acceptance**

Foreign collecting agents acknowledge receipt of items for collection by letter. Upon the receipt of such letters they are checked against the collection register and entry is made in the proper column therein. Whenever the foreign bank



has a time item for collection it advises the New York bank when acceptance has been obtained. This information is entered in the collection register and also on the reverse side of the debit ticket in the files. Advice of acceptance is sent to the owner on Form 40 which shows the bank's collection number, the client's collection number, the amount of the item,

THE NATIONAL CITY BANK OF NEW YORK					
FOREIGN DIVISION					
TO <u>Consolidated Tape Co.,</u>				NEW YORK <u>March 3, 1921</u>	
<u>149 South Street, New York.</u>					
WE TAKE PLEASURE IN ADVISING THAT YOUR COLLECTIONS HAVE BEEN ACCEPTED TO MATURE AS FOLLOWS					
YOUR NO	CAR NO	DRAWEE	AMOUNT		DUE
7853	99999X	Delville Hermanos	500	00	April 5, 1921

*J. P. White*  
THE NATIONAL CITY BANK OF NEW YORK  
FOREIGN DIVISION

Form 40 Advice of Acceptance of an Export Collection (Size  $8\frac{1}{2} \times 5\frac{1}{4}$  )

the correspondent's name, where drawn, the date of acceptance, and the due date

### Follow-Up of Unpaid Items

It is in the best interests of the customer of the bank that the collection be effected and funds placed at his disposal in the shortest time possible. To make sure that collections are being attended to promptly by foreign collection agents a follow-up system for delayed items is maintained. A diary is kept in which are entered under the heading of each business day the collection number and the amount of all items which should be heard from on that day. This diary, or tickler,

is checked against the disposition column of the collection register. If an item is found to be entered in the collection register as paid for or as returned unpaid it is crossed off the diary. If, however, no such entry is found in the collection register investigation is necessary. Mention has already been made of the fact that information regarding the progress of items through the collection process is entered on the reverse side of the debit tickets in the files. From the information contained on the corresponding debit ticket, therefore, it is possible to determine whether an outstanding collection is receiving proper attention. If such is not the case inquiry is made of the foreign collecting bank either by mail or by cable as the circumstances require. The item is then advanced in the diary to the date when response to the inquiry should be received. This follow-up process is repeated at intervals, if necessary, until disposition of the item is finally effected.

### Settlement Between the Banks

The two banks which are parties to the collection transaction make settlement between themselves after collection has been effected or it has been definitely established that collection cannot be made. Assuming that collection has been successfully made, the foreign bank sends the New York bank a letter or cable advising it of the collection and indicating the method which it is using to reimburse the latter bank.

The foreign bank may handle the transaction in one of three different ways, according to arrangements previously made:

- 1 It may request the New York bank that its deposit account with this bank be charged for the proceeds
- 2 In case the foreign correspondent is one with which the New York bank maintains a credit balance, it may place the proceeds to the credit of the New York bank
- 3 It may make remittance in New York exchange

*Charge Basis—Due to Foreign Banks and Branches* Whenever the account of the foreign bank is to be charged the debit ticket is completed by entering such information as the date of the foreign letter of advice, the foreign bank's collection number, and the value date, the last-named term signifying the date upon which the charge to the foreign bank's account is to be effective. After the adequacy of the balance has been determined, this ticket is sent to the bookkeepers where it is entered to the debit of the account of the foreign bank.

*Charge Basis—Due from Foreign Banks* In case the foreign bank has credited the proceeds of the collection to the account of the New York bank maintained with it, which is the usual procedure in case of foreign currency items, the charge ticket is completed as described in the preceding paragraph and it is sent to what is known as the "due from foreign banks" section of the books where it is debited to the bank's account maintained with the correspondent abroad. At this point it should be remarked, in anticipation of what is to be said in the chapter on the work of the foreign bookkeepers, that the bank maintains two classes of foreign accounts. First, there is the "their" account, or "due to banks—foreign," section which contains the accounts of foreign banks maintaining a balance on deposit with the bank. These accounts are the exact counterpart of the domestic customers' accounts. The second section of the foreign books, entitled the "our" accounts, or "due from banks—foreign" section, contains the accounts of those foreign banks with which the bank maintains a credit or deposit balance. This class of accounts has no counterpart in the domestic business because it is the policy of the bank to maintain a credit balance with no domestic correspondents. These accounts are, however, similar in a way to the bank's account with the local federal reserve bank, with the difference, of course, that they are

kept in the currency of the country where the foreign bank is domiciled

*Remittance Basis.* Collection items for which the foreign bank remits, instead of giving credit, are charged to the collection ledger of the foreign division until the book has received the remittance. When received the remittance is credited to the collection ledger offsetting the charge which has just been described.

### Unpaid Items

Unpaid items are returned by the collection agent together with the reason for non-payment and a bill for whatever charges it has made. In making collections of domestic items correspondent banks do not usually charge each other for their services in attempting collections. In foreign banking, however it is the general rule to make a charge for such services whether collection is actually effected or not. In addition, there are such charges as protest fees, cable charges, bill taxes, etc. Charges of this sort are usually credited to the account of the foreign collection agent and reimbursement obtained from the owner of the item by charging his account or by calling on him for a remittance to cover it.

Before a foreign bank returns items unpaid, it customarily gets into touch with the New York bank and these two banks then endeavor to adjust any differences which may have arisen between the drawer and the drawee of the items. Every possible effort is made to close out the transaction without necessitating the return of the item unpaid.

### Settlement with Owner

Settlement with the customer is effected by crediting his account or by sending him a cashier's check for the proceeds of the collection. The credit ticket and advice of payment, which were partially prepared at the time the item was sent

out for collection, are completed at this time. Upon them are entered details of the charges which were deducted, including the New York bank's commission, correspondent's commission, stamp charges, discounts and deductions authorized by the owner, cable charges, exchange charges, etc. The nature of these various charges is signified by their names, with the possible exception of charges for commission. Commission

THE NATIONAL CITY BANK OF NEW YORK <i>Foreign Office</i>	In reply kindly refer to Our No F C <u>999999E</u>
Advice of payment to be mailed to	New York <u>April 30, 1921</u>
<u>Consolidated Tape Co.</u> <u>149 South Street, New York City.</u>	Drawn by <u>Same</u>
We wish to inform you that the following collection has been paid, drawn on <u>Bogota, Colombia</u> against <u>Delvalle Hermanos</u>	
Sent us in your letter of <u>Jan. 5, 1921</u> your No <u>7853</u>	
Amount of draft <u>500.00</u> less charges abroad <u>\$3.38</u> we credit your account \$ <u>496.62</u>	
Tenor <u>120d - date</u> <u>1/5/21</u>	
Foreign Collection Dept Export	
By <u>J. P. White</u>	

Form 41 Advice of Payment of an Export Collection. (Size 6 x 4)

is charged only on dollar items and includes the charges of both the foreign correspondent and the domestic bank for their services. After the proceeds of the collection item have been determined the amount is entered upon the credit ticket and this ticket is carefully checked before it is sent to the bookkeepers for entry. The credit may be made either to a customer's account or to the Cashier's Check account, depending upon the method of payment used. The letter of advice (Form 41) is then completed and mailed to the customer to serve either as an advice that credit has been made to his

account, or as a letter accompanying the cashier's check which is being sent him

### Conversion of Foreign Money

As has already been stated, in many cases the foreign item will have been drawn in foreign money and will have been credited on the books of the foreign bank in foreign currency rather than in dollars. Such an item, after collection has been effected abroad, is treated as foreign exchange to be purchased. The foreign exchange traders of the bank, who fix the rates of exchange for all transactions, furnish a conversion rate for such items. This rate includes the commission charge. The owner of the item is then paid the proper amount in United States money.

### Collections by Cable

It sometimes happens that a customer of the bank desires especially rapid collection service. In such a case the bank handles the advice from abroad by cable, the owner of the draft or the drawee paying for the cost of the message. There are three methods of handling collections by cable:

- 1 Cable payment
- 2 Cable proceeds
- 3 Cable transfer

*Cable Payment Method* In handling a collection by the cable payment method the foreign bank advises the New York bank by cable that collection has been effected and that the proceeds are being forwarded by mail in the case of dollar drafts, or that they have been placed to the credit of the New York bank abroad if the draft was drawn in foreign currency. Upon receipt of this cable message the New York bank communicates the contents of the cable to the owner. By such a method the owner of a foreign draft is advised

promptly that his drafts are being honored abroad. He is also assured that funds are in the hands of the collecting banks and that he will receive them in due time. An assurance of this kind is of advantage particularly to exporters who have other shipments ready to go forward to the foreign drawee, but who do not desire to extend the additional credit which would be required were additional shipments sent forward before the proceeds of past shipments were in the hands of the collecting banks.

Aside from its value as an assurance that drafts are being honored, the cable payment may also be used to place the owner of a collection in funds. In advising the payment abroad of a foreign currency item the bank sends the owner a quotation at which it will immediately purchase the item. If the customer so desires he may sell the proceeds immediately at the current rate without being put to the necessity of waiting until funds arrive from abroad.

If the draft is drawn in dollars the customer may discount it with the foreign discount department upon the receipt of the cable announcing payment. Arrangements for such a discount are often made at the time the draft is entered for collection. In such a case the transaction is turned over to the foreign discount department upon the receipt of the cable announcing payment and the latter department then handles the transaction as it does other foreign discounts. (For a discussion of procedure in discounting foreign drafts, see pages 284 *et seq.*) If arrangements for discount were not made when the item was entered for collection, the owner is at once informed that payment abroad has been made. If he desires the collection discounted the owner then advises the bank to that effect.

*Cable Proceeds Method* For items drawn in dollars other methods of settlement can be used to make the owner's funds available to him immediately after collection, namely, the

cable proceeds method and the cable transfer method. These two methods of handling collections are identical excepting that the owner pays the cost of sending the funds under the cable proceeds method, while the drawee pays them under the cable transfer method. It is evident that only collections drawn in dollars can be handled in these ways, since it is only in case of dollar items that actual transfers of funds are made. In collecting foreign currency items the proceeds of all drafts are placed to the credit of the New York bank's account abroad when collected. If it were desired to make proceeds of such collections immediately available to the owner, such items could only be handled by the cable payment method, since no actual transfer of funds takes place.

In making a collection on a cable proceeds basis the foreign bank collects from the drawee in the usual way, that is, it collects at the sight rate of exchange on New York City. It then deducts from the amount collected the difference between the sight and the cable rate, and cables the New York bank to make payment to the owner of the amount so obtained. This method virtually amounts to discounting the collection item for the number of days the funds would normally be in transit from the city of the drawee to the city of the drawer.

*Cable Transfer Method* If proceeds are to be sent on the cable transfer basis, the drawer of the draft has an understanding with the drawee to the effect that the latter will pay the amount of the draft at the *cable rate* for exchange on New York prevailing in his city at the time of collection rather than at the sight rate. In other words the drawee pays the draft by purchasing a cable transfer from the foreign collecting bank. When this transfer reaches New York the local bank pays the owner the face of the item less the usual collection charges, that is, he is under no additional expense by virtue of the funds having been sent forward immediately by



## IMPORT COLLECTIONS

## Foreign Collections Department

The other phase of the foreign collection service is represented by the work of the foreign collection import department. This department of the New York bank performs a function in connection with outgoing collections of foreign banks which is the exact counterpart of that which these foreign banks perform for the New York bank in connection with its export collections.

Collections which come into the foreign collection import department are similar to those which are sent out by the foreign collection export and the foreign discount departments. They consist of items which have been taken by foreign banks in their collection or other discount service and which are being sent to the New York bank for collection. All incoming collections are payable in the United States. They are received through the mail as a general rule, but occasionally they come over the window. This often occurs when a foreign concern has an agent or a branch in the United States and it desires its branch or agent to enter a domestic item for collection and credit to the foreign account. Incoming items are accompanied by the regular letter of transmittal which contains the instructions of the foreign bank as to how the item is to be handled.

## Receiving Clerk

Incoming items first come to the attention of a receiving clerk. It will be recalled from the description of the letters of transmittal in the work of the foreign collection export department that remittance letters always go forward in duplicate or in triplicate. The receiving clerk lays aside the duplicate and triplicate letters for consideration after the originals have been worked up. Each item is stamped with a

time stamp to indicate the time of receipt. The letters are then sorted according to the division of labor which obtains in the department. This division is according to customers served. Separate forces handle items coming from customers located in cities appearing under the alphabetical classification A-B, C-G, H-L, M, N-S, and T-Z.

### **Cash and Collection Items**

The material is divided into two classes: cash items, and collection items. The cash items are those which are to be credited to the accounts of the senders upon the date of receipt, while collection items are those which are to be credited when collected. The cash items are thus to be handled practically on a deposit basis. Accordingly the work of the foreign collection import department in handling these items is similar both in practice and in functional significance to the work of the domestic mail teller. Cash items include only clean drafts which can be collected by the bank within one day, excepting items coming from its own foreign branches. A foreign branch, to meet the competition of branches of other American banks, receives immediate credit for all checks drawn upon the receiving bank, all clearing house checks, sights, trusts, items drawn upon the United States Treasury, and transit items, while foreign customers receive immediate credit for all the above-mentioned items except transit items. All other items are regarded as collection items, for example, bills drawn in foreign currencies, time items, documentary drafts, and transactions in which the bank is requested to make delivery of valuable papers and documents against receipt or payment, i.e., collection items not represented by a draft.

### **Separation of Cash from Collections**

The first work of the various operating divisions is to separate cash items from collection items. This is accom-

plished by making a physical separation of the items themselves into the two divisions and by removing the collection items from those letters which also contain cash sendings. As in the case of the domestic mail teller's work, incoming letters fall into one of three classes: letters containing only cash items, letters containing only collection items, and letters containing both cash and collection items. The letters containing only cash items are separated from those containing only collection items. On the mixed letters the different collection items are indicated by encircling them with a colored pencil and the cash items are footed in color. The collection items from these mixed letters are then entered on special interdepartmental letters. The mixed letters, upon which only cash items now have a significance, are placed with the other purely cash letters. Opposite each cash item the class of funds it represents, such as check drawn on the receiving bank, clearing house check on bank No. , sight, trust, etc., is entered on the remittance letter for reference.

Cash items from this point on are handled as ordinary deposits. The letters are proved against their contents in batches. Then they are passed to the bookkeepers for credit to the accounts of the owners. The enclosed items become material for the domestic departments of the bank to handle in the regular way: the checks drawn upon the receiving bank for the check desk, clearing house checks for the racks, sights, trusts, and U. S. Treasury items for the city collection department, and countries for the transit department—to be collected by those departments in the regular way.

### Advices of Credit

In the meantime triplicate letters advising the foreign customer that his account has been credited are prepared. These letters are held until sufficient time has elapsed for unpaid items to be returned through the regular channels. Should

none be returned unpaid the letters of advice are forwarded to the customer, the originals by one mail and the duplicates by another, but in case some items are unpaid, correction is made by charging back the unpaid ones and advising credit of the balance, if any. Thus the advice of credit is sent only after the bank is certain that nothing will have to be charged back. In case of cross-credits, i.e., items sent by one customer for the credit of another, the bank advises both the sender and the customer whose account is credited.

### **Import Collection Register**

Each collection is assigned a serial number which is stamped upon each of the constituent items. This number becomes the identification number of the particular transaction. A collection register is kept which is similar in form and in function to that of the export collection department. Each transaction is entered in this register in a space which has been previously stamped with the serial numbers to be borne by collection items. This book contains such information as: customer from whom the item has been received, for credit of whom, amount of item, tenor, maturity, place payable, customer's number, documents, etc. Space is also provided for making entry of the date of the acceptance (in case time items are sent for acceptance) and for indicating the fate of the item after collection has been attempted.

### **Conversion of Foreign Currency Items**

Many of the incoming collection items are drawn in foreign currency. Local drawees, however, make their payments in the currency of their own country. This situation necessitates the conversion of the face amount of items of this sort from foreign currency to domestic. In case the foreign sender has not already made this conversion, a conversion rate is obtained from the traders of the bank and the

amount to be collected is indicated in dollars on the face of the item.

### Collection Through Domestic Departments

Incoming foreign collection items require exactly the same type of collection service as do domestic collection items. To have the foreign collection import department effect the actual collection of its receipts would mean wasteful duplication of work within the bank. To avoid this the items are forwarded to the various domestic departments of the bank, each item being described by its collection number. The domestic departments attempt to effect collection and they report the fate of the items back to the foreign collection import department, using the collection number again for describing the transaction. The transaction is then completed by making settlement with the client in accordance with his wishes. In keeping with this arrangement acceptances are sent to the note teller, items to be collected or accepted by drawees located in the city to the city collection department, out-of-town collection items to the country collection department, and city coupons to the coupon collection department.

### Customers' Cards

It is highly desirable for the bank to know the amount of business which it has transacted for each of its foreign customers, also the amount of collections outstanding for each account and the time when the proceeds of these outstanding items may be expected to be added to the accounts of the customers. To obtain this information entry is made on customers' cards, as illustrated in Form 42. Cash items are entered in red ink, while collection items are entered in blue. These cards contain the following information: date received, collection number, customer's collection number, letter date, where payable, tenor, and amount. There is also space for

FOR CREDIT TO THE ACCOUNT OF <i>National City Bank of N.Y. of Buenos Aires, Argentina</i>						
DATE REC'D	OUR NO.	THEIR NO.	LETTER OF	WHERE PAYABLE	TENDER	AMOUNT
3/1/21	27654	41144	2/1/21	J. P. Moore, Boston	60	25,000.00
3/1/21	27655	41145	2/1/21	Johnson, Chicago	60	5,250.00
3/1/21		41146	2/1/21	No 23		500.00
3/1/21		41147	2/1/21	No 4		3,000.25
						323.00
						323.01
						330.14
						333.10
						Discounted 3/1/21
						Paid
						Paid
						Paid.

Form 42 Customer's Card for Import Collections (Size 9 3/4 x 11 3/4.)

indicating the receipt of duplicates as they come in and for indicating the fate of the item after collection has been made

### Settlement with Owner

Day by day the domestic departments of the bank complete collections for the foreign collection import department. In disposing of the proceeds from such collections the domestic department sends the bookkeepers a ticket crediting the collection account of the foreign remitting bank or individual and forwards an advice of collection to the foreign collection import department. The cash items received from the collection pass through the domestic work along with the other cash or cash items received.

Upon receipt of the advice of payment from the domestic department the transaction is completed. Letters of advice are prepared for the foreign customer in duplicate. These advices are proved against the notices received from the collecting department. They are also used by the clerk in charge of the collection register to make entry in the register as to the fate of the collection. The advices to be sent to the foreign customer are then carefully checked before they are forwarded abroad. In case instructions have been received to this effect, advice of payment is sent by cable rather than by mail.

The advice of payment received from the domestic collecting department, from which the letters of advice for the customer were prepared, now becomes a credit ticket destined for his deposit account. The domestic collecting department has listed the net amount of the proceeds on the ticket. The foreign collection import department fills in the name of the customer to receive credit and a complete description of the item. It then deducts the bank's commission for effecting the collection, which it credits to the Commission account. The net amount remaining is sent through to the foreign bookkeepers as a credit to the deposit account of the foreign cus-

tomers As an offsetting entry to this credit ticket a ticket charging the collection account is put through, since this account was credited at the time collection was effected by the domestic collecting department.

### Unpaid Collections

Items which the drawees refuse to pay are handled in about the same way as are unpaid items in the domestic collection work If the item amounts to \$500 or more it is the regular policy of the bank to cable non-payment to the owner, in the absence of instructions to the contrary. In all other instances the instructions of the foreign customer govern the action of the department It is often possible for drawees and drawers of foreign drafts to communicate with each other and adjust their differences In order to accommodate its clients the bank holds unpaid items for sufficient time to enable the owners and the drawees to settle differences if they care to do so The owner of the item then instructs the bank as to what course is to be pursued After it has been definitely established that a collection will not be paid, the item is returned to the owner together with an advice of debit to his account for the expenses incurred in attempting collection In addition to the regular expenses of protest fees, bill stamps, cable charges, etc., it is customary for banks to make a nominal charge for attempting collection, as was noted in connection with the foreign collection export work.

### Time Items

Frequently time items are received upon which the bank is requested to procure acceptance, to deliver documents in return therefor, and after acceptance either to collect or to discount the item In transactions of this sort the bank sends a special advice of acceptance to the owner The resulting acceptances are collected through the note teller's department



or discounted with the domestic discount department, according to the instructions of the customer

### Discounts

Items for discount may arise in two different ways In the first place the foreign customer often sends instructions, either special or standing, to have items discounted The standing instructions of customers are quite frequently to the effect that acceptances entered by them for collection are to be discounted in amounts sufficient to restore their balances in case they fall below a certain stipulated amount In the second place the bank quite frequently discounts acceptances for customers whose accounts show an overdraft, regardless of whether it has instructions to do so or not This acts as a protection to the customer in that his drawings are protected in case of need It may be assumed that he would readily give instructions to have such action taken were he communicated with In connection with these discount items it should be remarked that they are for the most part either bankers' acceptances or acceptances of the very best commercial names in the country Many are acceptances of the bank itself Such paper makes an ideal investment from the standpoint of the bank because of the high degree of security, and from the standpoint of the owners in that they are enabled to obtain a very satisfactory rate

Discounts of this sort are handled after the regular manner of domestic discounts An offering slip containing information regarding the amount of the bill to be discounted, name of the owner, name of the drawee, and tenor is prepared and submitted to the officers of the bank If it is accepted for discount the rate is determined and the offering slip completed by entering the rate on the ticket Three officers are required to place their signatures on the slip as authority for completing the transaction

### Records Pertaining to Discounts

Letters of advice of credit for the proceeds of discounts are prepared. These instruments go forward to the customer in the regular way. The items themselves are sent to the domestic discount department where they are handled as a part of its regular work. The foreign collection import department keeps certain auxiliary records of its discount operations. One set of records consists of a card (Form 43) giving a list of the bills discounted for each bank or individual and containing the following information: date discounted, foreign bank's collection number, New York bank's collection number, drawee, due date, date paid, face amount, rate, and net amount. In addition to serving the purpose of indicating the volume of business transacted for each customer, these records show the outstanding contingent liability of foreign customers upon discounts. Cards of a separate color are kept for the discounts made for the foreign branches of the bank.

Another set of records consists of the drawees' cards (Form 44). This record serves the purpose of giving the amount of liability to the bank of different drawees, upon bills discounted. They contain the same information as is to be found on the owners' cards. As in the case of the owners' cards, a separate card shows the business of each drawee or acceptor.

### Duplicates

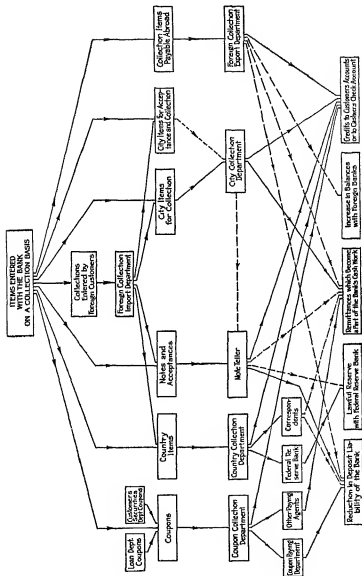
Finally, a word should be said regarding the duplicate and triplicate of remittances which are received from the foreign clients. The status of any copy of a foreign item is worthless if some other copy has already been received and honored, while it is to be treated as the valid copy providing other copies have not been received. In order to ascertain whether other copies have been received the clerks refer to the account cards previously mentioned and if there is no record of such having

Bills Discounted for Account of <i>National City Bank of N.Y. of Buenos Aires, Arg.</i>									
DATE DISCOUNTED	OUR NO.	THEIR NO.	DRAWEE	DUE DATE	DATE PAID	FACE AMOUNT	RATE	NET AMOUNT	
5/10/21	27654	41144	J. B. Morris Boston	July 4		25,000	6%	24,770.83	
5/10/21	27698	42958	J. B. Morris New York	July 5		6,500	6%	6,402.50	
5/12/21	29101	64753	J. W. Mellon & Co. N.Y.	July 27		150,000	5 1/2%	149,702.52	
5/13/21	29191	64794	J. A. Grant Chicago	July 4		72,000	6%	71,376.00	

Form 43 Discount Card for Import Collections (Size 11 1/2 x 9 3/4)

Bills Discounted Drawn on <i>J. B. Morris of Boston, Mass.</i>									
DATE DISCOUNTED	OUR NO.	REMITTER'S NO.	REMITTER	DUE DATE	DATE PAID	FACE AMOUNT	RATE	NET AMOUNT	
3/10/21	27654	41144	J. B. Morris Buenos Aires, Arg.	May 4		25,000.00	6%	24,770.83	
3/26/21	29976	43678	J. E. Smith of Rio	June 6		100,000.00	6%	99,400.00	
6/14/21	42762	65491	Lloyds London	Sept 12		90,000.00	6%	88,650.00	

Form 44 Drawee's Card for Import Collections. (Size 11 1/2 x 9 3/4)



Form 45 Chart Showing Disposition of Items Entered by Customers for Collection

Broken line debits show the various disposition of such collection items when a debit may be made in more than one way

been entered the copy in question is collected in the usual manner. If, however, a prior copy has been entered the clerks stamp a number on the item and file it for future reference. Special instructions from the drawee or the indorser may lead the department to dispose of the duplicates otherwise. If the originals have not been received, presentation and demand for payment of the duplicates is made, they being handled just as though they were the originals. When, if ever, the originals of these transactions arrive they are handled as duplicates.

At this point description of the collection work of the bank has reached completion. The routine of the complete collection work of the bank and the disposition of the various items entered by customers for collection is given on the chart shown in Form 45.

## CHAPTER IX

### CREDIT

#### Controlling Investment Operations

Before describing the investment operations of the bank, which consist mainly in making various kinds of loans, it is necessary to consider the process of controlling these operations. There are two phases of the work. The first consists in gathering and filing information affecting the credit of borrowers. In the United States the bank loan is very frequently unsecured, that is, the safety of the loan lies in the ability and willingness of the borrower to repay rather than in collateral security of some sort. In addition, a bank is vitally interested in knowing what use is to be made of the funds it loans, hence the importance of a bank's having adequate and reliable credit information. The work of gathering and filing this information is performed by the credit department of the bank. The second phase of controlling loans consists in analyzing credit information and passing upon applications for loans. Because of its outstanding importance this work is performed wholly by certain officers of the bank.

#### Sources of Credit Information

1 *Banks* The bank uses every available source of information in obtaining and compiling credit data. Other banks constitute one of the important sources. So far as the confidential nature of the information which they possess permits them to do so, banks in the United States quite freely exchange experience on credit matters with each other. Accordingly the bank obtains information from other banks through correspondence and through calls made by its domestic field men

and city investigators. In the foreign field the credit departments and field men of the branches of the bank are most useful sources of information and this is supplemented by that received from time to time by correspondence from foreign correspondent banks.

2. *The Trade.* Another important source of credit information is the trade—those who buy and sell merchandise or who have other business dealings with the applicant for credit. Those who sell to the subject of an investigation have the same problems confronting them as the bank has and a knowledge of the circumstances under which they extend credit to him is very valuable. Likewise competitors and others not dealing with him direct are, nevertheless, in a position to give the bank accurate information as to his standing in the trade. By exchanging information with certain of the large commercial concerns the bank is enabled to obtain very close and reliable information upon the business ability and integrity of the subject as well as the credit rating which he enjoys among his business associates.

3. *The Applicant Himself.* Another important source of information is the subject himself. It is the usual practice for customers, especially those who desire a direct line of credit at the bank, to give complete information about themselves to their bankers. One medium for obtaining a personal contact with the applicant for credit is the letters and the personal interviews of the officers, industrial engineers, and field men of the bank. Another is the financial statement submitted by the subject. Practically every applicant for accommodation submits his periodical financial statement to his bank in support of his claim for credit. By analyzing the statement the bank is enabled to obtain very accurate and close information regarding the merits of the customer's claim to credit.

4. *Credit Agencies, Clippings, and Brokers.* Still other

sources of credit information are the commercial credit agencies. To supplement other sources of credit data the credit department also maintains a clipping bureau which obtains from newspapers and periodicals such information as new organizations, consolidations, changes in corporations and firms, also death notices, notices of dissolution, lawsuits, judgments, bankruptcy proceedings, etc. Each of certain employees in the department regularly reads one or more designated newspapers or trade publications from which he clips any news items having a bearing upon the credit rating of those with whom the bank deals and of other important houses. Another important source of information consists of commercial paper brokers. It is customary for these dealers to furnish the banks which patronize them with complete and reliable information about each concern whose notes they handle.

5 *Past Relations with the Applicant* Finally the bank considers the history of its past relations with the applicant, if it has had dealings with him previously. Such information as the customer's average balance, the amount of borrowing which he has done in the past and under what conditions, what he owes the bank directly or indirectly, whether or not the account has been overdrawn, profitability of the account, amount of gratuitous service furnished, etc., provides a very reliable index as to the desirableness of that particular subject as a credit risk. Whether or not the applicant does the whole of his banking business with the bank is also an important factor to be considered.

### Credit Folder

Credit information is filed in what is known as a credit folder. The completeness with which the information contained in these folders is gathered depends upon the relations which exist between the bank and the particular subject to



which the folder pertains. In the case of those who borrow from the bank in the domestic or foreign departments the information is as elaborate and complete as it is possible to make it. The bank also keeps information of the same degree of completeness of those concerns whose notes it purchases either for itself or for its customers through the note brokers. In the case of concerns other than borrowers the information may be slightly less complete. Except when information is given to it confidentially the bank, however, disseminates credit information about such names as these as a business service to its clients and it often uses this information as a basis for soliciting new business. Accordingly, while the files upon these names are not quite so complete as those concerning borrowing accounts, they are kept up to date.

### Contents of Credit Folder

The typical credit folder consists of nine sections as follows:

- 1 The fly sheet
- 2 Discount or loan ticket section
3. Financial statement section
4. Information section
- 5 Interviews
- 6 Credit information
7. Inquiry section
- 8 Credit agency reports
- 9 Correspondence and miscellaneous.

*Fly Sheet and Discount Ticket Section.* The fly sheet contains certain salient points concerning the subject of the folder. This consists of the name and address of the company, a list of the officers or members, kind of business engaged in, date the account was opened, by whom introduced, officer accepting the account, accounts maintained with other banks,

note broker, if any, through whom it sells paper in the open market, indorsers or guarantors whose names it has agreed to furnish on its borrowings, the line of credit extended to the concern by the bank, and names of concerns affiliated with it. The discount and loan ticket section contains the completed offering tickets which, as will be noted presently, have been prepared in connection with each discount and loan made to the subject. Since these tickets contain complete details of each borrowing made by the customer in the immediate past, the officer who is examining the folder with a view to making a loan to the applicant has at his disposal in this section of the folder a complete borrowing history of the account.

*Financial Statement Section* The statement section contains the original financial statements received by the bank together with summaries prepared by the accounting division of the credit department. The original statement may have been prepared by the applicant himself or it may have been prepared and certified to by a public accountant. This statement is submitted either upon the subject's own form or, preferably, upon a form especially designed by the Federal Reserve Bank of New York with a view to facilitating credit analysis. A division of the credit department known as the accounting division transfers the information contained in the statement to the bank's own special comparative form (Form 46) which shows changes in the concern's condition from one financial period to another. The comparative statement also includes a summary of the condition of the subject at the time his last statement was made. This summary of condition shows the date of statement, total quick assets, current liabilities, percentage of quick assets to current liabilities, deferred liabilities, total liabilities, net worth, annual sales, and net profits of the concern.

*Remaining Sections* The information section of the

## COMPARATIVE STATEMENT

Name THE JOSE TOR MANUFACTURING COMPANY,

Endorse

Address NEW YORK CITY

Reference

Business Manufacturers of Felt Hats

Account

Metropolitan Trust Company  
Federal National Bank

N Y C

Description	Date	P. R. Form		Direct-Receipt			
		Oct. 31, 1925	Jan. 1, 1926	Oct. 31, 1925	Jan. 1, 1926		
<b>CURRENT ASSETS:</b>							
Cash		37,915		25,922			
Accounts Receivable—(Merchandise)	A	779,864	*EA	807,912			
Notes Receivable—(Merchandise)	A	100					
Trade Accounts Receivable	A	2,081	*EA				
Drafts against Foreign Deposits							
Merchandise—Finished	J	85,907	G	18,019			
Merchandise—Unfinished	J	405,040	D	807,400			
Raw Material							
U. S. Liberty Bonds		866		972			
Bar Certificates							
<b>Total</b>		<b>1,211,713</b>		<b>1,630,725</b>			
<b>Fixed Assets—Tangible Assets All I</b>							
Real Estate		20,000		20,000			
Buildings	JB	127,428	JB	146,840			
Machinery, Furniture and Equipment							
Goodwill, Patents, etc.	*	249,000	*	249,000			
Due from Officers, Employees, etc.							
Investments in Affiliated Companies		125,562	L	10,000			
Other Loans, Bonds, etc.		10,345	K	19,258			
Deferred Charges							
Advances to Debit & Company			X	128,212			
<b>Total</b>		<b>412,335</b>		<b>323,058</b>			
<b>Total Assets</b>		<b>1,624,048</b>		<b>1,953,783</b>			
<b>CURRENT LIABILITIES</b>							
Accounts Payable		27,954		230,808			
Notes Payable to Other Banks		275,000		230,800			
Notes Payable through Banks							
Notes Payable for Merchandise				50,618			
Notes Payable to Others				125,234			
Trade Accounts Payable							
Due from or to Banks for Foreign Credits							
Receipts for Taxes		102,701	D	114,452			
Dividends Payable							
Wages and Salaries a/o-Not due		64,549	F	70,388			
<b>Total</b>		<b>440,204</b>		<b>646,208</b>			
<b>DEFERRED LIABILITIES</b>							
Banked Date (due)							
Marques and Loans (due)							
<b>Total</b>		<b>0.00</b>		<b>0.00</b>			
<b>CAPITAL SECURITIES</b>	Preferred	250,000	I	250,000			
Common		232,500	IG	232,500			
Surplus and Unassigned Profits		434,548		475,275			
<b>TOTAL LIABILITIES</b>		<b>672,752</b>		<b>913,983</b>			
<b>6/70, 7/50-</b>							
Selling Times		20					
Annual Sales		2,778,118					
Net Profits		1,804,579					
Dividends Paid		20,000					
Withdrawals by Partners							
Cash on Hand at End of Year							
Income: First on Buildings		31,127					
Machinery, Fuel, and Exp.		300,000					
First on Merchandise							
Life		50,000					
<b>RECAPITULATION:</b>							
Total Current Assets		884,360		1,371,821			
Total Current Liabilities		1,025,500		1,115,193			
Net		371,860		256,628			
Ratio		1.79		1.36			
Total Assets		1,624,048		1,953,783			
Total Liabilities (in Capital, Surplus and Unassigned Profits)		672,752		913,983			
Net		951,296		1,039,800			
Compared Liabilities							
Official Liabilities—Maritime	4-2-	647,722					
Official Liabilities—Maritime	2-2-	134,978					

folder contains reports which have been received from banks, the trade, and other references which have been given by the subject or have been consulted by the bank, records of interviews which the bank's officers have had with the subject, and mounted clippings from newspapers and periodicals. The

KEY									
A—Reserve for Doubtful Receivables detailed as follows:									
Accounts Receivable			\$ 2180						
Notes Receivable	net							35916	
Trade Acceptances	net								
B—Reserve for Depreciation detailed as follows:									
Buildings		44	211						
Machinery and Fixtures		160	311					217028	
C—Treasury Stock detailed as follows:									
Common								14000	
D—No reserve reported									
E—Cost									
F—Market									
G—Full of value not reported									
H—Further information desired									
I—Capital Authorized:									
Preferred 5% Cumulative								250000	
Common								250000	
J—Valued at cost or market whichever is lower									
K—Trade Acceptances Receivable								37,320	
Accounts Receivable								216,437	
Total Receivables								253,757	
Less—Reserve								30,716	
								307,913	
L—Capital stock investment in Dehne & Company									
M—25 shares C. J. Heikla Company preferred stock.									
N—Includes U. S. Government Bonds loaned then in amount of									
								30,000	
O—Reserve for State and Miscellaneous Taxes									
Reserve for Inc. & Excess Profits Taxes—1918								1,438	
Reserve for Inc. & Excess Profits Taxes—1920								76,000	
								30,000	
								114,438	
P—including an unspecified amount of local taxes									

Form 46 (b) Comparative Statement of a Corporation (reverse)

representatives' reports and memorandums sections consist of reports of the bank's domestic field men and foreign branch bank credit and field men regarding the outcome of the investigations which they have made. In the inquiry section is filed a list of those making inquiry regarding the subject,

dates of inquiries, and references to the form letters written in reply. In this section the bank also files copies of the replies which it has made to such inquiries. The agency section consists of reports received from commercial credit agencies. The correspondence and miscellaneous section consists of correspondence regarding terms arranged between the concern in question and the bank, also other letters which would be useful in quickly ascertaining the status of transactions passing between the subject and the bank.

### Credit Files

The credit files are separated into two divisions, the domestic and the foreign, and each of these divisions is divided into subsections—individuals (including individuals, firms, and corporations), and banks.

In the domestic section the folders are filed alphabetically according to names in the case of individual folders, and according to cities in the case of banks. The foreign files are divided into five sections and are arranged alphabetically in each section, namely, Caribbean, Russian-Asiatic, Scandinavian, South American, and European. In addition to that containing active material there is a very extensive file containing material which has gone out of date and which has been superseded by new matter. This old material is transferred to a file warehouse where it is kept for a considerable period before it is destroyed.

To facilitate locating a particular folder in the file and to keep a check on the filing records a card index is maintained. One section of the index pertains to the domestic files and the other to the foreign files. The cards are filed alphabetically.

Because of the very intimate nature of the material contained in the files, strict regulations are enforced regarding the consultation of the folders. The file clerks are responsible for keeping the information contained in the files from the

eyes of unauthorized persons. Folders are given out only upon requisition signed by an officer of the bank or by some other authorized person. The requisitions are attached to cards which are placed in the files to replace folders which have been withdrawn. The outstanding folders are checked up at frequent intervals and steps taken to have them returned to the department as quickly as possible.

### Revising Information

Both regular and special revisions of the information contained in the credit folders are necessary. It is the policy of the bank to revise its information upon each borrowing account as often as seems necessary. Special revision becomes necessary in case information is received which affects the rating of a subject adversely or in case the information obtained from two or more sources is decidedly conflicting in nature. Special investigations or revisions are also made whenever the bank receives requests for credit information which it cannot answer in a complete manner from the information on file.

In so far as is possible it is the custom to make the revision of borrowing account folders immediately after the receipt of the annual financial statements of the respective concerns or just before that time of the year when the customer usually arranges for his annual requirements at the bank. By experience the credit men can frequently estimate the time of year when accommodation will be asked for. Accordingly they make their revisions, if such are necessary, just before this request for the extension of credit comes in, in order that the information held by the department may be most pertinent to its chief function. The department also keeps a record of the time when borrowers issue annual statements and a part of the work of the revision consists in obtaining these statements promptly after they are issued.



should be mentioned that of furnishing credit information to customers and others as a banking service. The tendency is for credit men, both in banks and in other concerns, to avail themselves fully of the credit service of their metropolitan correspondents and to rely on them for information regarding those to whom they propose to extend credit. To a correspondent of the bank this is a great service when it has under consideration the extension of credit or the purchase of commercial paper or when it is called upon by its customers for information which it does not have in its own files. Commercial houses, of course, find the bank an important source for information regarding those to whom they propose to sell on credit. The service is also particularly important in connection with foreign trade. American concerns desiring to transact business with foreign merchants and foreigners wishing to deal with American traders find the credit department of a large bank which has not only extensive foreign correspondent connections but also special representatives, agents, and branches located abroad, almost indispensable to the successful consummation of their dealings. The policy of the bank upon the practice of which this study is founded, is to disseminate credit information as freely as is possible, due regard being had, of course, to the confidential nature of the material on file and to the reliability of the applicant for such information.

The department gives out information regarding credit risks preferably in writing or by personal interviews. When it becomes necessary to send a letter regarding a credit risk it is customary to use what is termed "non-liability" paper. This paper contains a statement as follows:

All persons are informed that any statement on the part of this bank, or any of its officers, as to the responsibility or standing of any person, firm, or corporation, or as to the value of any securities, is a mere matter of opinion, and



given as such, and solely as a matter of courtesy, and for which no responsibility, in any way, is to attach to this bank or any of its officers

Occasionally it is necessary to answer inquiries by telephone, but in that event the credit man first assures himself of the identity of the person to whom he is speaking

In case the bank does not have sufficient data for the needs of the one making the inquiry it makes a special investigation. Charges are made for these investigations where cable or telegraph fees are incurred, otherwise the service is gratuitous, as the purpose underlying such accommodation is service to the customer rather than profits. The bank, of course, has the benefit of this information for its future use

### **Approval of Commercial Paper Names**

An important phase of the credit service of the bank arises in connection with commercial paper. The services of the bank in purchasing commercial paper in the open market for its customers has already been explained. This service may consist in actually making the purchase or in recommending certain offerings for direct dealings between the broker and the prospective purchaser. In any event, the most important part of the service consists in passing upon the credit rating of the makers of paper. Requests for services of this sort are made to officers of the bank who make selections with the aid of the credit folders with the same care as they would in choosing paper for the bank's own portfolio

### **Use of Credit Information in Making Loans**

The chief purpose in obtaining credit information is to control loans. After credit information has been gathered the first step in the operation of extending bank credit is for the banker to decide whether he cares to extend credit to the applicant, and if so, how much

The matter of passing upon applications for credit and fixing the lines to be extended rests with certain officers of the bank. For the purpose of securing efficient administration the business of the bank is divided on a territorial basis. A domestic territory consists of certain states which are not only geographically contiguous but in which economic and business conditions are the same. A foreign territory contains certain countries grouped together on this same plan. Each territory is under the direct control of a vice-president of the bank assisted by other officers. All matters involving the bank's relations with a customer come to the attention of the officers of the territory in which the particular customer is located. In this way direct personal relations are maintained with each client.

The most important work of the territorial officers consists in passing upon the applications of the customers of their territories for credit. Each application comes directly to the attention of the vice-president in charge of the territory. Co-operating with certain of his assistant officers who are trained credit men, the vice-president has the responsibility of passing upon the application.

### **Application Ticket**

The manner in which an application for credit is handled by the bank is as follows. When a customer applies to the vice-president in charge of his territory for a line of credit the application is passed to the credit department which prepares an application ticket (Form 48) containing the name and address of the applicant, kind of business engaged in, date of application, amount applied for, and, if the applicant is a bank, its capital, surplus, and undivided profits.

This ticket is sent to the domestic discount department. This department notes the amount owing to the bank by the applicant on account of discounts, together with maturities,

the date, rate, amount, and maturity of the last discount made for this particular customer, amount of discounts made during the previous year, when and how long the applicant was out of debt to the bank, and names of those authorized to negotiate loans and sign notes. The application ticket then goes successively to the loan department, the foreign discount department, and the commercial credit department where

7-942	
Offering by <u>George B. Thompson &amp; Co.</u>	Date <u>March 23-1921</u>
Address <u>New York City</u>	Business <u>Shoe Manufacturers</u>
Borrowing Authority? <u>None from Dept. of Finance</u>	Capital \$ <u>—</u>
Amount <u>150,000.00</u>	Character of Loan <u>June Maturities</u>
<u>Guaranteed</u>	Interest on balance <u>2%</u>
Maximum amount discounted last year <u>160,000</u>	Guaranty? <u>1/10/18 200 MC</u>
When out of debt and how long (discounts) <u>Sept 1/20 to Oct 2/21</u>	Continuous? <u>Yes B. Thompson</u>
Maximum amount of loans last year <u>0</u>	<u>I. R. Bryant</u>
When out of debt and how long (loans) <u>0</u>	
Maximum amount borrowed at one time last year <u>150,000</u>	When due <u>June 7, 1921</u>
Liability under Travelers Letters of Credit <u>0</u>	Last Rate <u>6 1/2%</u>
Present amount of discounts <u>130,000</u>	Date <u>Feb 2-1921</u>
Liability as endorser <u>0</u>	When due <u>—</u>
Purchased paper <u>0</u>	Last Rate <u>—</u>
Present amount of Loans <u>0</u>	Date <u>—</u>
Present amount with Foreign Exchange Dept. <u>13,733</u>	
Average balance for past six months <u>149,500</u>	
Average balance for same six months last year <u>167,300</u>	
Balance to-day <u>100,422.65</u>	
APPROVED <u>[Signature]</u>	CR. DEPT. <u>[Signature]</u>

Form 48 Application for Line of Credit (Size 8 1/4 x 5 1/2)

similar information regarding the applicant's borrowings in these departments is added.

The ticket is then returned to the credit department, which keeps a card file showing the balances kept by each customer. From the file is obtained the customer's average balance for the last six months, average balance for the corresponding six months for the previous year, the balance on the date of application, and the rate of interest, if any, allowed applicant on his balances. A credit man then scrutinizes the application, approves it for correctness of the information contained

therein, and returns it, together with the credit folder of the applicant, to the officer who is to pass upon it

### **Analysis of Credit Information**

In discussing the analysis of credit information, emphasis should be placed upon the fact that each application is considered on its own merits. Many intangible factors have to be taken into consideration so that it is difficult to generalize to any great extent in pointing out the factors which are considered. The work cannot be standardized. In the following paragraphs, however, the most important general considerations are given.

The important points considered in analyzing a credit risk are the character, capacity or ability, and capital of the applicant—"the three C's of credit," as they are termed. It is difficult to say upon which of these factors the banker lays most stress. He considers them all essential. Character, however, is undoubtedly the basic element, while ability is a close second. Often the situation presents itself wherein a concern whose capital is not at all extensive is enabled to obtain credit merely upon the bank's confidence in the character and the ability of the principals. On the other hand, credit is never granted to a concern the character of whose managers the bank has reason to doubt, regardless of the capital which they may have accumulated.

### **Character and Capacity of Applicants**

There are no formulas for analyzing the character and ability of an applicant for credit. However, it may be said that before reaching a final decision the credit man takes into full consideration all those intangible factors upon which success in business ultimately rests. For that reason the applicant's personality, his standing in the business and social community, his attitude toward his obligations, his ability as a

manager, his relations with employees, etc., are considered. As already indicated, much information about these things is gathered by the credit department by inquiry among the various trades and by correspondence with other banks—in fact, by consulting all those in whose judgment confidence may be placed and who may have been in a position to form an opinion relative to the applicant for a loan. Whenever possible, however, it is always preferable to supplement these sources by a personal interview with the applicant, for in this way the officers are able to gain such a direct impression of both character and ability as may serve as a basis for all future relations between them.

### **Analysis of Financial Statement**

To form an estimate of the financial condition of the applicant the credit man relies to a great extent upon his financial statement made out upon an approved form such as the federal reserve statement illustrated in Form 49. All conditions being equal the bank prefers to receive from its customer an audited statement, this preference is not due to any doubts concerning the honesty of the applicant, but is due rather to the fact that the audited statement presents credit information in a uniform and readily comprehensible manner. An audited statement is an especially reliable source of credit information if the audit is made by a firm of accountants specializing in the particular kind of business which is being audited.

It is well at this time to indicate briefly the points which the banker considers in analyzing the financial position of an applicant for credit. Customers generally submit a balance sheet together with a condensed profit and loss statement covering their operations for a certain fiscal period. The balance sheet indicates the assets under the headings of "quick assets" and "fixed assets." The term "quick assets" includes

## CONFIDENTIAL

Federal Reserve Bank of New York, Statement Form, Accepted  
CORPORATION

Statement of THE YORK ICE MANUFACTURING COMPANY.

Business MONTHLY STATEMENT OF ASSETS Address NEW YORK CITY.

TO THE NATIONAL CITY BANK OF NEW YORK

For the purpose of procuring credit from time to time with you for any negotiable paper or otherwise we furnish the following as a true and correct statement of our financial condition on DECEMBER 31, 1934. We agree to and will notify you immediately in writing of any materially unfavorable change in our financial condition and in the absence of such notice or of a new and full written statement this may be considered as a continuing statement and substantially correct and it is hereby expressly agreed that upon application for further credit this statement shall have the same force and effect as if approved as a correct statement of our financial condition at the time such further credit is required.

(PLEASE ANSWER ALL QUESTIONS AND FILL IN ALL BLANKS)

ASSETS		LIABILITIES	
Cash on hand and in Banks	70,914.00	Accounts Payable, incl. div.	27,817.75
Accounts Receivable for Mfg. and	272,354.00	Notes Payable to our Banks, incl. div.	273,000.00
Other Accounts Receivable	0.00	Notes Payable through Banks	0.00
Notes Receivable for Mfg. and	300.00	Notes Payable for Merchandise	0.00
Other Notes Receivable	0.00	Notes Payable to Others	0.00
Trade Acceptances Receivable, incl.	1,329.08	Trade Acceptances Payable	0.00
Drafts against Foreign Shipments	0.00	Due to Banks as Backers for Foreign	0.00
Merchandise—Finished	85,906.72	Credits	0.00
Merchandise—Unfinished	455,644.55	Deposits of Money with us	0.00
Raw Material	0.00	Labour and Salaries Accrued, incl. div.	24,569.47
U. S. Liberty Bonds	0.00	Reserves for Extra Profit, Interest	1,021,903.25
Other Cash Assets (Sundry)	66.00	Other Taxes	0.00
1918 War Certificates	0.00	Dividends Payable	0.00
		Other Current Liabilities (Sundry)	0.00
Quick Assets	558,120.25	Current Liabilities	420,392.45
Real Estate	50,000.00	Bonded Debt	0.00
Machinery, Plant and Equipment	1,374,400.43	Mortgages and Loans	0.00
Goodwill, Patents, etc.	340,000.00	Other Liabilities (Sundry)	0.00
Due from Officers, Employees, etc.	0.00		
Investments in Affiliated Companies	1,085,562.06	Current and Deferred Liabilities	420,392.45
Other Stocks, Bonds, etc.	0.00	Capital Stock Preferred	250,000.00
Deferred Charges	1,024.83	Capital Stock Common	250,500.00
Other Assets (Sundry)	0.00	Surplus and Undivided Profits	434,642.35
TOTAL	2,358,370.04	TOTAL	2,358,370.04

Merchandise, On what basis valued, cost, market or selling price  
Cost or market, whichever is lower.

If any merchandise is held on consignment, state amount and  
circumstances None.

Notes and Payable for year ending with date of this statement.  
If it falls \$2,229,119.00. Net profits \$148,455.39.  
Dividends Paid \$ 25,000.00.

Accounts and Notes Receivable. If any are past due or doubtful  
state amount and circumstances. \$12,000.00 will  
be paid. \$12,000.00 will be paid. \$12,000.00 will be paid.  
If any accounts are due from directors, officers, employees, sub-  
sidiary or similar persons, state amounts, security  
and circumstances None.

On What Terms Do You Sell? 6/10, 5/10 = 5%

Stocks and Bonds. State general character and whether readily  
salable at value stated. None except stock of sub-  
sidiary company, the value of \$100,000.00.  
Total value \$100,000.00.

Insurance. Fire on Buildings \$ 200,000.00. Machinery, Plant and  
Equipment \$ 200,000.00. Merchandise \$ 200,000.00.  
Life in favor of Company \$ 50,000.00.

We hereby certify that the foregoing figures are taken from the books of this Company and that they and the statements are  
based on books of this Company and are true and give a correct picture of the financial condition of this Company.

Signed this 31st day of December 1934.

THE YORK ICE MANUFACTURING COMPANY.  
By WILLIAM BROOKS TREMPER  
(State official title)

(OVER)



such items as cash, accounts receivable, merchandise, raw material, etc., which in the regular course of the applicant's business will be liquidated in a comparatively short time. Fixed assets, on the other hand, consist of real estate, plant and machinery, good-will, etc., which constitute the permanent capital of the concern in an economic sense. The intention is not that such fixed assets shall be liquidated but that they shall rather be used permanently to facilitate the operations of the owner. Liabilities, also, are divided into current liabilities and fixed liabilities. Current liabilities consist of notes payable, accounts payable, etc., which in the regular course of business will have to be paid off in the near future, while fixed liabilities consist almost entirely of long-term bonds and mortgages which have been issued to cover certain of the fixed assets.

### Cash Account

In analyzing a concern's cash account the banker likes to know whether, perchance, there are included such items as demand notes or I O U's, covering withdrawals, expenses, or loans to members or employees of the concern. The banker looks upon the custom of carrying such items in the cash account as an unfavorable sign. He also desires to know whether any part of the cash is held by affiliated or subsidiary companies under the so-called "imprest cash system," or whether any part of it is held on deposit by questionable concerns in process of liquidation. The credit man also interprets the cash account in the light of the conditions obtaining in the business at the time of taking the statement. The account may be unusually large at statement periods on account of pending distributions for dividends or for salaries. While this is in no sense a questionable practice, frankness in noting such a fact on the financial statement is an important consideration.



### Notes Receivable

The credit man ascertains whether the item of notes receivable in a financial statement includes only strictly trade notes given for actual purchases, or whether it covers loans to officers or employees, subscriptions for stock, accommodation notes, notes of affiliated concerns, hypothecated notes, etc., which may be uncollectible in case of failure. The credit man also interprets the size of the notes receivable item in the light of the custom prevailing in the applicant's line of business. If it is customary to take buyers' notes in that particular line of business, the Notes Receivable account may well be large, as a general rule, however, a large item of notes receivable is unfavorably received. Likewise long-term notes are not good assets to loan money upon because of their slowness of maturity.

### Accounts Receivable

Regarding the item of accounts receivable, it is important for the credit man to know which, if any, of the accounts included are those due from affiliated concerns or from persons closely associated with the business. The credit man also determines whether any of the applicant's accounts receivable have been hypothecated.

The applicant's practice in regard to bad and worthless notes and accounts is a very important consideration in judging his worth as a credit risk. The credit man favors a conservative attitude on the part of the concern; this attitude is expressed in a policy of charging off bad accounts and setting up a reserve for those which may prove uncollectible in the near future.

The liquid condition of accounts receivable is indicated by the proportion due from customers for merchandise recently sold, which accounts can reasonably be expected to be settled according to the terms of sale. The proportion of past-due

accounts indicates the effectiveness of the collection methods of the applicant for credit

### **The Inventory**

In considering the applicant's inventory the banker desires to know what basis has been used in arriving at the figure given—whether the inventory was figured at cost or at the market price, whichever happened to be the lower at the time of taking stock. The concern's practice in regard to old stock is also an important index to its credit rating. It is a healthy sign from the standpoint of the credit man to see such goods eliminated from the live assets of the concern either by charging off the proper depreciation or by closing them out by means of special sales. The banker also interprets the inventory in the light of the nature of the goods which it covers, making allowances for such merchandise as luxuries, novelties, etc., for which there is not a constant demand or a ready market.

### **Stocks and Bonds**

The most important point to be considered in connection with stocks and bonds for investment is the purpose which prompts the concern to carry them as an asset. While an asset of this sort may indicate a speculative tendency in the business, such is not always the case, and if these items are readily salable they strengthen the credit standing of the owner. Government bonds, particularly, are considered strong liquid assets, and they are usually shown as quick assets in a statement. Stocks and bonds of affiliated or subsidiary companies are naturally not favored so much in passing upon an application as are those of independent concerns. In cases of this sort credit men ascertain the relationship existing between the two concerns and whether the one has any contingent liabilities or contracted obligations to the other incurred through the ownership of such securities.

### **Real Estate**

In connection with the applicant's real estate and plant the credit man seeks to determine whether mortgages are outstanding against such property, whether it is in good operating condition and well adapted for the business, whether the property is amply protected by insurance and well located with respect to transportation and labor supply, whether any unpaid taxes, assessments, or other liens are outstanding against it, and also whether it is adaptable for other than its present use. The policy of the concern as to providing for depreciation is also important.

### **Machinery and Fixtures**

An item of machinery and fixtures of a standard character with some value in case of liquidation is of far greater value to the credit man than is a similar item of an equal cost which would have to be scrapped in case of liquidation. In fact, the considerations which apply to a factory building apply almost entirely to machinery and equipment.

### **Sundry Assets**

Among the sundry assets on a financial statement the credit man considers insurance and the other deferred charges, if they represent actual unexpired values. Good-will, patents, trademarks, leaseholds, etc., are of varying value from a credit standpoint and there is a growing tendency to eliminate these items entirely from a balance sheet or to carry them at a nominal value.

### **Self-Liquidation of Assets**

The essential consideration in connection with a concern's assets is their power of self-liquidation within a reasonable time, for the banker is chiefly interested in knowing that the

customer can pay his loans from the normal fruits of his operations. Therefore the bank's credit man concentrates his attention mainly upon current assets.

### Notes Payable

Among the quick or current liabilities of a firm, notes payable is a most important item. Knowing the practice in a given trade, the banker expects the item notes payable given in payment of merchandise to be small except in those very rare cases in which it is the established custom of the business to purchase on notes rather than on open account. If notes are given for overdue accounts it is considered a bad sign by the would-be grantor of credit. The banker also checks up the amount of notes given to banks for borrowed money and the amount which has been sold through the note brokers, and he is constantly on the alert to determine the security of outstanding notes.

Occasionally a concern will have outstanding notes secured by collateral or indorsed or guaranteed by individuals interested in the business, and it will seek to borrow from its bank on its unsecured note. This practice, of course, restricts the line of credit which the bank will grant. Notes payable, representing loans or advances from officers, directors, members of their families, or other persons closely associated with the company, may indicate an additional security in that those interested in the business are willing to risk their money in it, on the other hand, there is a possibility that those closely associated with the principals may be in a position to gain advance information of impending danger and thus withdraw to the detriment of other creditors.

The use to which a concern puts the funds which it borrows is also important. Legitimate uses for funds obtained from a bank are considered to be, for settling open accounts, taking discounts on purchases, and for manufacturing or

operating outlays On the other hand it is not always considered good policy to borrow on short-time loans for the purpose of adding to slow assets

### Accounts Payable

The credit man is desirous of knowing what amount of accounts payable represent trade obligations, what accounts are past due, if any, and which ones are secured in some manner It is also important for him to know what amount is due to affiliated concerns, officers or directors, employees, members of their families, or others closely associated with the business.

### Bonded Indebtedness

Fixed liabilities include mainly bonded indebtedness, although current instalments of bond issues are considered as belonging among the current liabilities The banker is interested in knowing whether the bonds are amply secured by mortgages, otherwise they constitute a lien upon the general assets of the concern and in the event of liquidation the unsecured residue would share equally with the claims of other creditors The amount authorized, the total amount issued, the maturity dates, and the purpose for which the bond issue was made, are important for obvious reasons Provision for retirement of the bonds together with the extent to which a concern is living up to sinking fund requirements, if there are any such requirements, is also an important item

The credit man is particularly desirous of knowing that all assets and all liabilities, particularly the latter, have been indicated in the statement Such contingent liabilities as notes receivable discounted, accommodation notes, indorsed notes, and other items of this sort which do not always appear upon the financial statement, have frequently been the means of ruining a concern and occasioning a heavy loss to those extending credit to it

### **Analysis of Profit and Loss Statement**

In connection with the profit and loss statement several items are important from the credit man's viewpoint. The banker is interested in knowing whether the net profits are commensurate with the volume of business and the amount of capital employed. The policy of a concern as to making provisions for depreciation, bad debts, etc., is an important index not only to its actual financial condition but also to its business policy. Aside from being bad business, the policy of paying dividends excepting out of the profits of the current period or out of a comparatively large surplus is considered decidedly derogatory to the credit standing of a concern. Sales and profits for the period under consideration are compared with those for corresponding periods in the time past, the purpose being, of course, to determine whether the concern is going forward or backward. Lastly, a favorable attitude on the part of a concern toward accumulating a surplus to provide additional working capital is considered an indication of favorable conditions for granting credit.

### **General Impressions of Statement**

Certain general points and comparative figures taken from the applicant's balance sheet are extremely important in determining the line of credit the bank is willing to extend. The manner in which a statement is made gives an insight into the business methods and practices of the proprietor. The credit man considers that a statement which is complete and clear in every detail—one which brings the unfavorable points into equal prominence with the favorable ones—is worth more from a credit standpoint than a garbled or ambiguous one which shows on its face a better financial condition. The credit man also considers the degree of co-operation which the customer shows in furnishing a statement of his affairs promptly and in assisting in the analysis of doubtful points, if necessary.

The time of making a statement is important, too. Statements are often drawn up at the time of lowest indebtedness of the firm and at times when large cash accumulations are on hand, which are soon to be disposed of for salaries, dividends, etc., and the credit man takes such facts into consideration in analyzing credit data.

### Financial Position Expressed in Ratios

Certain ratios are also very important. The annual sales as compared with the terms of sale indicate how profitably the capital of the applicant is being employed. The ratio of quick assets to current liabilities is always made much of by the credit man of the bank. Bankers usually like to lend upon a ratio which shows 2 to 1, or better. However, in many lines of business as small a ratio as  $1\frac{1}{2}$  to 1, or even less, has been found to be satisfactory. No hard-and-fast rules can be laid down regarding this ratio. The facts of the case are always to be interpreted according to the nature of the applicant's business.

The ratio of cash to bills and accounts payable indicates the adequacy of the applicant's balance maintained in the bank. The annual rate of turnover also becomes an important figure to the bank credit man. These rates of turnover vary materially from business to business, but from long experience with many concerns in different lines of business the banker comes to know the proper rate of turnover for each line and he is thereby enabled to judge whether the applicant's rate is normal or not.

### Financial Statements of Banks

The foregoing applies more properly to individuals, firms, and corporations not engaged in the banking business. In analyzing the statement of a bank the ratio which capital and surplus bear to deposits, the aggregate size of its capital, sur-

plus, and deposits, and the ratio of this aggregate to the bank's loans and investments, are important elements to be considered in connection with the bank's claim for a line of credit. The cash on hand and the amount of outstanding bills payable are also very carefully considered. The relation between these items varies from bank to bank in different sections of the country, and the credit man interprets them in the light of the peculiar conditions prevailing in the locality.

### Line of Credit

A favorable decision to grant credit to an applicant is expressed in a line of credit or a loan agreement. A line of credit may be defined as an agreement on the part of the bank to carry loans up to a certain maximum at any given time for the beneficiary. In other words, borrowers commonly provide in advance for the banking accommodations which they need for a season and the line of credit represents the bank's agreement to furnish such accommodation or a portion of it. The line of credit is subject to revision on the receipt of each annual statement and at any time during the interval, in the event that the credit standing of the beneficiary undergoes an important change.

### Agreements Under a Line of Credit

The bank makes certain stipulations when granting a line of credit. The line generally carries with it agreements as to indorsers and collateral. It is also understood between the customer and the bank that average balances approximating 20 per cent of his line of credit will be maintained. This does not mean, however, that the borrower does not have the use of the full amount of his deposit balance should need arise, for the bank does not object to letting his balance fall below 20 per cent. It asks only that he restore his balance when he is in possession of funds to a point sufficiently high



to maintain an average for the period of the life of the credit line equal to 20 per cent. If a customer prefers, the bank lends him five times the amount of the average balance which he has maintained for the 6 months prior to the time of granting the loan within the limits, of course, of the maximum line of credit granted. Stipulation is also made that the borrower be entirely out of debt to the bank for a reasonable period of time during the year, inasmuch as the bank considers that this provision insures the liquidity of its assets and indicates that the funds are being put to proper use.

### Application for Loan—Offering Ticket

When the borrower submits his application for a loan to be made under the line of credit the bank examines the application, or offering, as it is called, in about the same way that it examines the original application for the line of credit. The officer who receives the application submits it to the credit department which prepares an offering ticket to be sent to the domestic discount department, the loan department, and the foreign departments of the bank. In these departments information of the same sort as that indicated upon the ticket which was circulated in connection with the application for a line of credit is entered, in fact the same form is used in both cases. After this offering ticket has been returned the credit department returns the application to the officers who have charge of the applicant's territory. After having approved the application these officers submit it to the officers' meeting for review and send the transaction to the operating departments for action.

By way of summary it may be said that the work of the credit department and of the groups of officers results in the authorization of the loan. This function is performed in three phases: the investigation, the fixing of a line of credit, and the approval of the offering. The approved transaction

then becomes the raw material for the work of such operating departments as the domestic discount, the foreign discount, the loan, and the commercial credit departments which are to be described in the chapters just following

## CHAPTER X

### DOMESTIC DISCOUNTS

#### General Statement of Discount Operations

A most common form of loan in the domestic banking practices of the United States is the discount. This consists of an advance made by a bank against an instrument maturing some time in the future, the bank's charge for this service being deducted at the time the advance is made. The discount differs from what is termed technically a loan in that on the discount the bank's charge is collected in advance while on the loan it is collected at intervals after the advance is made and at maturity. For example, if a customer of the bank borrows \$100,000 on his note running for 3 months on a discount basis at a rate of 6 per cent the bank advances him \$100,000 less its charge of \$1,500, or \$98,500. At maturity the borrower pays the face of the note, or \$100,000. If the same note is handled on a loan basis the bank advances \$100,000 at the time of making the loan and it receives \$101,500 at maturity. The domestic discount is also generally unsecured, that is, it is made on the credit rating of the borrower re-enforced in some cases by indorsements. The loan, on the other hand, is generally secured by some form of collateral—stocks, bonds, warehouse receipts, bills of lading, etc.<sup>1</sup>

To understand the significance of unsecured discounts in the domestic financial practices of the United States it is necessary to examine briefly the methods of financing which give

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<sup>1</sup> From a strict departmental standpoint these distinctions do not always hold good. On some items handled by the domestic discount department the bank's charges are not collected in advance while on some handled by the loan department the charges are collected in advance. Also some transactions handled by the domestic discount department are secured by collateral, notably receivables.

rise to them. In a work of this sort only general types of financial operations can be indicated, for practices differ widely from trade to trade and, to a certain extent, from concern to concern in a given trade.

### Open Book Account

The most common practice is for the seller of merchandise, of raw material, etc., to sell his goods on account, the terms varying from, say, 10 to 90 days. The purchaser is generally given the privilege of paying cash within 10 days for which he is allowed a discount termed a "cash discount" ranging from  $\frac{1}{2}$  per cent to 5 or 6 per cent, or even more. This open book account transaction gives rise to two types of borrowing. The first type of borrowing arises from the fact that many buyers do not take advantage of the cash discount terms offered by sellers and they accordingly have to be carried by the sellers until such time as their obligations mature and are paid. Sellers usually finance a transaction of this sort by borrowing at their banks, most frequently upon their unsecured notes, in an amount sufficient to carry their open book accounts for the season. The second type of borrowing arising from the open book account transaction comes from the desire of buyers of merchandise to take advantage of cash discount. In order to be able to do this these buyers, too, generally borrow of their banks upon their unsecured notes.

### Financing of Receivables

In some trades it is customary for the buyer to give promissory notes in settlement of his purchases. These are time obligations and have to be carried to maturity just as do open book accounts. The seller in this case usually finances the transaction by borrowing from his bank upon his unsecured promissory note an amount sufficient to enable him to carry these notes, termed "receivables," until maturity. Occasional

the seller discounts the receivables themselves at his bank in order to raise funds to finance his operations

### Trade Acceptances

Another method of financing commercial transactions consists in the use of the trade acceptance. The purchaser of a bill of goods is required to accept a time draft for the amount involved. This instrument, termed a "trade acceptance," has the same status as the promissory note or the receivable. The owner of such paper carries it in one of the ways mentioned in connection with financing receivables. He discounts it at his bank, or he borrows upon his note an amount sufficient to enable him to carry it in his portfolio to maturity.

### Borrowing in Open Market

In describing the methods of financing just mentioned it was presumed that the borrower goes directly to his bank for his needs. Occasionally, however, concerns finance their transactions by selling through note brokers large blocks of notes in round denominations made by themselves or by certain of their large customers. Note brokers act as middlemen, purchasing the notes of large borrowers and selling them at the best rate obtainable to banks or other financial institutions with surplus funds to invest. This form of financing is termed "borrowing in the open market."

### Single- and Two-Name Paper

The notes and acceptances arising from the foregoing credit practices fall into two classes: the single-name, and the two-name paper. Single-name paper is that for which one party only is liable for payment, while two-name paper is an instrument carrying the obligation of a drawer in addition to that of an acceptor, or of an indorser in addition to that of a maker. Thus the trade acceptance is always two-name paper,

as is also the receivable when discounted at a bank. The borrower's unsecured note is, on the other hand, single-name paper.

### **Safety of Unsecured Commercial Loan**

As has been indicated, much of the paper discounted by banks consists of what is known technically as "unsecured" paper. It must not be thought, however, that there is no security behind loans made in this way. Broadly speaking, the security of such paper as a class rests upon the purchasing power of the community at large. As surely as the consuming population will be able to pay for that which it purchases, so surely will borrowers be able to liquidate the loans which they negotiate to finance such transactions. The security of the individual loan within the class is, of course, the credit standing of the borrower. Many concerns are known to fail even when they have no difficulty in disposing of their products—in fact, many become overextended at such times, hence the importance of carefully analyzing the credit standing of each individual borrower.

### **Domestic Discounts**

The department within the bank which is responsible for putting into effect the instructions of the officers with reference to the negotiation of instruments payable in the United States is known as the domestic discount department. Under the arrangement which is in effect the officers fix the lines of credit which make up the general limit for the operations of the loaning departments and in the case of domestic discounts they pass upon each individual transaction. The domestic discount department therefore, as well as other departments through which credit is extended, becomes solely an operating department. Accordingly the function of the domestic discount department is to care for all notes and acceptances dis-

counted and commercial paper purchased by the bank for its own account. On instructions from the executive management this department also prepares commercial paper for rediscount with the federal reserve bank.

### Domestic Discount Department

Specifically, the operation of handling a domestic discount may be divided into six component parts, as follows:

1. Entering items, which consists in calculating the proceeds and making settlement with the borrower.
2. Caring for the item and the collateral, if any.
3. Collecting maturing items.
4. Accounting for the income from discounts.
5. Attending to rediscounts and pledges of commercial paper.
6. Keeping records and preparing statistics and reports for the directors.

Items offered for discount and commercial paper purchased in the open market for the bank's own account are approved by the officers having charge of the territory of the borrower who indicate their approval on an offering slip as was stated in the preceding chapter. This slip contains, in addition to approval of the offering, full instructions as to amount, maturity, rate, and the other terms under which the loan is to be made. The offering slip therefore accompanies the item for guidance in entering the discount. After it has served this purpose it is sent to the credit department to be filed in the borrower's credit folder.

### Discount Blotter

Discounts are first entered in a blotter. The purpose of this book is to give merely a preliminary record, it constitutes a book of ready reference to all items which may not have

reached the stage of the work when they are entered on other records. This record is useful in checking up the progress of the work, in gathering information regarding unentered credits to accounts which appear overdrawn, etc. The offerings are entered consecutively as they are received and such information as the time to run, date, amount, and rate is shown on the pages of this book.

After entry in the blotter the notes are timed. The timing procedure has the same significance as in the work of the note teller, that is, it signifies finding the due date and indicating it on the face of the items.

### Calculating Discount

The discount is computed by hand, that is, without the use of interest tables. For the term of discount the actual number of days which the item has to run before maturity are taken. The rate is that indicated by the officers on the offering slip. The base of the calculation is the amount due upon the note or acceptance at maturity. The characteristic item of the discount operation is the non-interest-bearing note; hence the amount upon which the discount is calculated is generally the face of the note. Otherwise it would be the face of the note plus interest due at maturity. While banks count the actual number of days to run in arriving at the term of discount, they consider the basic interest year as consisting of 360 days. Thus if on March 1, 1920, a note for \$5,000 dated as of the discount date, due in 90 days without interest, were offered for discount at  $5\frac{1}{2}$  per cent, the calculation would be as follows:

$$\text{Discount} = \frac{5,000 \times 90 \times .055}{360} = \$68.75$$

$$\text{Proceeds} = \$5,000 - \$68.75 = \$4,931.25$$

and this amount would be paid the customer



### Exchange Charges and Bill Stamps

In addition to the discount, the exchange charges which must be assessed upon those relatively few notes which are payable out of town, according to the requirements of the New York Clearing House Association, are deducted in arriving at the proceeds available for the customer's use. In the case of most notes, even if they are made by out-of-town makers, the bank has the maker give it authority to charge the item to his account upon the date of maturity. Such notes are accordingly payable in New York City, a discretionary point under the rules of the clearing house, and the bank is enabled to save the customer the exchange charge. In case the borrower has not already attached the necessary amount of bill stamps to the item offered for discount, the bank attends to this work, charging him for the amount of stamps furnished.

To make sure that the items have been accurately timed and that exchange charges, bill stamps, and especially discount computations, are correct, the clerk who makes these computations passes his work to a second clerk who goes over the items again. Before the discount is accepted in every particular a representative from the signature control department also examines it for genuineness of signature, in practice, however, he makes his examination on the day following the discount of the items.

### Discount Tickets

After the items have been timed and the proceeds calculated, tickets covering the details of each transaction are prepared. These tickets (Form 50), which are made in triplicate, contain the following information: name of customer, rate, date, due date, amount, discount, stamp charges, exchange charges, and proceeds. The original copy of this ticket, which is mailed to the customer at this time, serves as a statement

of the transaction and also as a reminder that he must have the necessary funds at the proper place of payment when the

THE NATIONAL CITY BANK OF NEW YORK STATEMENT OF DISCOUNT							
NEW YORK March 22, 1921. To Omega Manufacturing Co., New York City.							
RATE	DAYS	DUE	AMOUNT	DISCOUNT	STAMPS	EXCH	PROCEEDS
6	48	May 7	10,000.00	76 66	2.00		9,921 34

Form 50 (a) Discount Ticket (original) (Size  $7\frac{1}{4} \times 4$ )

Checked by THE NATIONAL CITY BANK OF NEW YORK STATEMENT OF DISCOUNT							
NEW YORK March 22, 1921. To Omega Manufacturing Co., New York City.							
RATE	DAYS	DUE	AMOUNT	DISCOUNT	STAMPS	EXCH	PROCEEDS
6	48	May 7	10,000.00	76.66	2.00		9,921.34

Form 50 (b) Discount Ticket (duplicate)

THE NATIONAL CITY BANK OF NEW YORK STATEMENT OF DISCOUNT						
NEW YORK March 22, 1921 CREDIT Omega Manufacturing Co., New York City.						
PROCEEDS OF NOTES DISCOUNTED						
						PROCEEDS
	May 7	10,000.00	76.66	2.00		9,921.34

Form 50 (c) Discount Ticket (triplicate)

note or bill falls due The second copy of the ticket is for use in making the proper book entries This copy is attached to the discounted item itself which it accompanies through the

work, afterwards it is filed as a record of the transaction. The borrower receives the proceeds of his discount either in the form of a cashier's check or, more frequently, a credit to his deposit account, hence the triplicate serves the function of a credit ticket for the purpose of crediting the proceeds to the account of the borrower or to the Cashier's Check account, as the case may require.

### Offering Book

Each transaction is entered in the offering book. This book is a most important record. In the first place it serves the function of a day book, showing the complete details of

BILLS DIS					
	Customer	Maker	Endorser	Payable	Rate
	March 7, 1921				
44	Grayson & Son	Our Note	J H Moore		6
"	Nantz & Co	" "			"
"	M P Strodel	" "	M O Dyke		"
"	J A Hartley	" "			"
"	J E Davidson	" "			"
"	Kauley & Phillips	" "			"
"	W S Prickett	" "			"
"	E H Morris	" "			"
"	R B Brown & Co	" "			"
"	"	" "			"
"	"	" "			"
"	"	" "			"
"	"	" "			"
"	W E Watson	" "	R M Mills		"
"	John Fox	" "			"



the debits and credits arising from the transactions. To record the charge to the proper asset account the face of the item discounted is entered in a column under the proper heading: Bills Discounted—Domestic, Bills Purchased, Acceptances of This Bank—Domestic, Acceptances of This Bank—Foreign, or Various Acceptances. As a matter of convenience the book is composed of three volumes, one for bills discounted (Form 51), one for commercial paper purchased, and one for acceptances. In this way the bills discounted and commercial paper purchased are charged by the use of one column in each of the proper volumes and the acceptances require only three columns in the last-named book.

Other columns in the offering book record the amounts of discount credited to the Discount Collected But Not Earned account, and the amounts credited to the Exchange account for exchange charges deducted. A column headed "Prepaid Expense—Revenue Stamps" contains credits to this account for the amounts of bill stamps used. Finally, two columns contain the credits arising in the two methods of settlement with the seller for the proceeds—credits to the Cashier's Check account and to the customers' deposit accounts. The footings of the respective columns indicate the changes in the accounts of the bank, and by entering these footings on the daily proof the necessity of preparing tickets covering each transaction is avoided. The sheets of the offering book are also sent to the weekly meetings of the directors of the bank, whose duty it is to establish the general policy of the bank in regard to making loans. After they have been approved by the directors, these sheets are returned and filed in a permanent binder.

### Discount Tickler

In order to bring maturities to attention on the proper date the notes and acceptances are recorded in a tickler which

also has an additional function in that it serves as a journal for recording credits arising from the maturity and collection of discounts.

There are two sections to the tickler—one for acceptances, and one for bills discounted and commercial paper purchased. Entries in the acceptance tickler convey the following information: the customer's name, name of the acceptor, place of payment, rate, earnings for one day; amount of acceptance, classified as Acceptances of This Bank—Domestic, Acceptances of This Bank—Foreign, Acceptances of Other Banks, Various Acceptances, and remarks. The tickler for bills discounted and commercial paper purchased contains for each item the name of the customer, name of the maker, place of payment, rate, earnings for one day, amount of the item, entered in separate columns according to whether it represents the borrowing of an individual account, a bank account, or purchased paper, and remarks. Items are entered in the discount ticklers according to maturity dates, just as are the notes of the note teller's department in the tickler of that department. Accordingly, when each business day arrives the corresponding page in the discount tickler shows the total amount maturing upon that day together with the journal entries necessary to take care of the maturities. The footings of the columns represent credits to the general accounts of the bank for the day's maturities.

### Discount Files

After entry in the various books of record the notes are placed in files which again are similar in purpose to the note boxes used by the note teller's department. The paper is filed in more detail, however, than is the case in the note teller's department for the reason that it may become necessary at any time to prepare certain classes and kinds of paper for rediscount with the local federal reserve bank, or for other purposes. The notes are, therefore, filed by grand sections

consisting of country items and of city items. The latter section is subdivided into (1) discounts and purchased paper, (2) acceptances of this bank, (3) acceptances of other banks, and (4) various acceptances. These subdivisions of the files enable the clerks of the department to locate readily any class of items desired. After the filing is complete the files are checked against the tickler, which in turn has been prepared from the offering book. This checking, therefore, insures the accuracy of the tickler, of the offering book, and of the filing of the notes at one and the same time.

### Collection of Discounts and Purchased Paper

The process of filing the notes completes the first phase of the work. The second and final phase consists of collecting matured items. Those payable in the city are collected by messenger. Country items are sent to the country collection department 10 days before maturity. This department effects collection in the usual way. The results of each day's collections are reported to the domestic discount department and incorporated in the latter's daily proof. Items made payable at clearing house banks are first presented to these banks for acceptance and then cleared the next day. Items payable at the bank itself and the bank's own acceptances are sent to the note teller who sends them to the check desk. Notes payable at the bank are charged to the accounts of the makers and returned to them among the canceled vouchers. The bank's own acceptances are then forwarded either to the export or the import commercial credit department, depending upon the nature of the acceptances, where the proper bookkeeping entries are prepared. The receipts of the domestic discount department—checks, currency, certified notes, etc.—are charged and sent to the note teller to be handled in his racks.

Since discounted items have become the property of the bank it is not necessary to credit depositors' accounts for collections as is done in the work of the note teller. The credits

arising from discounts which have been collected involve rather the asset accounts, Bills Discounted—Domestic, Bills Purchased, Acceptances of This Bank—Domestic, Acceptances of This Bank—Foreign, Acceptances of Other Banks, and Various Acceptances. These accounts being few in number, the credits are made in totals from the columns of the tickler, thereby obviating the necessity of making separate credit tickets for the proceeds of each collection.

### Unpaid Items

At the time of making a discount the bank takes every precaution to insure prompt payment at maturity, hence there is seldom any difficulty in effecting collection. The bank's own particular form of note which it requires borrowers to use in connection with their borrowings gives it certain privileges, among which is the right to charge the amounts of maturing discounts to customers' accounts. In a few cases, however, the accounts of customers may not show a balance for the time being sufficient to cover the amount of the note, or funds in the hands of other paying banks may not be adequate. In these cases the notes are carried until the officers of the bank can get into communication with the makers and arrange for the items to be met. If any of the unpaid items are acceptances or notes bearing indorsement they are protested for non-payment just as are collection items in the work of the note teller's department.

### Collection of Rediscounts

A word should be said at this point concerning the efforts which the bank makes to comply with the wishes of other banks in collecting paper which they rediscount with it. In a transaction of this sort the borrower signs an agreement permitting the bank to collect rediscounted items by charging them to his account and to reimburse itself for the original advance by presenting the rediscounts direct to the makers. The borrowing bank, however, in many cases does not wish



it to become generally known among its customers that items have been rediscounted. Such a bank accordingly indorses notes of this kind in pencil and requests the lending bank not to place its indorsement upon them. In making collection the bank affixes its indorsement stamp to a ticket attached to the item rather than to the item itself, and it sends the item to the borrowing bank for collection.

### Earnings of Discount Department

The earnings realized from the discounts are yet to be accounted for. The discount deducted at the time of discounting a note payable in 30 days, for example, is earned by the bank only after the 30 day period of discount has expired. As each day is completed, however, the bank earns one-thirtieth of the charge which it has already collected. Discounts collected from borrowers may therefore be considered as anticipated earnings, which become actual earnings as the periods of time upon which they are based expire.

To care for these anticipated earnings an account termed "Discount Collected But Not Earned" is credited for the amount of discount deducted on each discount. At the end of the fiscal month the amount actually earned is transferred from the Discount Collected But Not Earned account to the Discount account by means of bookkeeping tickets. When adjusted, the Discount Collected But Not Earned account is a liability account of the bank showing the aggregate amount of prepaid interest which the bank has yet to earn.

In arriving at the monthly earnings figure, computations of the amount earned each day are made. In the tickler and in the offering book the earnings for one day upon each item are indicated. Given the earnings figure for the preceding day, the earnings figure on discounts for any given day is obtained by adding to the given figure the total earnings for one day upon the new amounts discounted as shown by

the earnings column of the offering book, and subtracting one day's earnings upon the discounts which have fallen due according to the earnings column of the tickler for the given day. Due allowance is, of course, made for any discount adjustments made with customers during the day.

The amount of daily earnings is posted to a daily earned discount ledger kept in the department. This book contains three columns—one for debits, one for credits, and one for balances. One line is devoted to the earnings of each day, and one page to the earnings of each month. At the end of the fiscal month the total of the balance column shows the total earnings for that month. This amount is transferred to the accounts of the bank by sending to the general bookkeeper tickets debiting Discount Collected But Not Earned and crediting Discount account.

### Discounts Secured by Receivables

While as a general rule the domestic discount department does not handle loans secured by collateral of any sort, exception is made in the case of the borrowings of correspondent banks secured by receivables, because the collateral is the type of instrument which the domestic discount department is equipped to handle. The note, representing the obligation of the borrower, is handled in the regular way for discounts. The collateral, however, requires special attention. Mainly this is due to the fact that borrowers may wish to withdraw certain items contained in the collateral, substituting others therefor. Again, collateral notes often mature at an earlier date than the loan to the support of which they contribute.

Receivables of each bank are accordingly kept in a separate envelope where they can be readily located. These envelopes are ruled to show the amount and maturity of the loans, the amount of collateral received and returned, the dates, and the balance of collateral on hand. In the envelopes, receivables

are arranged in the order of their due dates, the earliest maturities on top. Tickler cards are used to indicate maturities of collateral.

Some time before collateral notes fall due the bank notifies borrowers of the fact. The object in doing this is to give the borrowing institution every opportunity to obtain its maturing receivables in time for it to present them to the owners for payment on the due dates. The bank cannot, however, release such collateral without receiving other security in its place, hence if the borrowing bank does not send acceptable substitute collateral promptly, the loaning bank protects itself by sending the maturing receivables to the borrowers to be collected for its account pending the substitution of other suitable items therefor. When the loan is finally paid, whatever collateral remains in the bank's possession is checked off the tickler cards and returned to the owner.

#### Rediscounts with Federal Reserve Bank

Under the provisions of the Federal Reserve Act certain of the notes and receivables held in portfolio by a member bank may be rediscounted with the federal reserve bank. The result of this legislation is to give to commercial paper all the qualities of an ideal secondary reserve. Member banks therefore quite freely rediscount their discounts with the federal reserve bank for the purpose of increasing their reserves or loaning capacity.

A member bank may borrow at the federal reserve bank either by rediscounting or by negotiating a loan secured by bonds or commercial paper. Paper which the federal reserve bank will accept for rediscount or as collateral security for a loan is termed "eligible" paper. What constitutes eligible paper is clearly defined by the Federal Reserve Act, the broader limits are set up in the act itself, while the narrower ones are left to be fixed by the Federal Reserve Board.

To be eligible for rediscount, an instrument must be a note, draft, or bill of exchange growing out of an actual commercial transaction. In order to conform to this requirement the instrument must have been issued or drawn for agricultural, industrial, or commercial purposes, or the proceeds therefrom must have been or are to be used for such purposes. The act specifically excludes instruments drawn for the purpose of carrying on trading in stocks, bonds, or other investment securities, except bonds and notes of the United States government or bonds of the War Finance Corporation.

The Federal Reserve Act further sets up a maturity limit for eligible paper. This limit is 90 days,<sup>2</sup> excepting for paper arising from agricultural and live stock transactions, which paper may have a maturity not exceeding 6 months.

Decisions to borrow from the federal reserve bank are made by the management of the borrowing bank, but the discount department is called upon to choose and prepare whatever commercial paper is to be used for securing the loan. Mention has already been made of the fact that the discounts are filed by classes to facilitate selecting eligible kinds. In addition to selecting the paper the discount department prepares an application for the loan according to the standard form prescribed by the federal reserve bank. This application contains a formal description of the accommodation asked for and of the paper offered for rediscount or as collateral.

### Accounting for Rediscounts

The book entry to record rediscount consists of a debit to the Prepaid Discount or Rediscounts account for the discount charge deducted by the federal reserve bank, a charge to Lawful Reserve with the Federal Reserve Bank of New York

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<sup>2</sup> In the wording of the Act (Section 13 Paragraph 4) member bankers except notes may have a maturity of 3 months.

for the proceeds, and a credit to Bills Rediscounted with the Federal Reserve Bank of New York for the face amount of the assets rediscounted. This last-named account represents the contingent liability of the borrowing bank as an indorser of the items rediscounted. At maturity and collection of the items rediscounted the contingent liability ceases. Entry is accordingly made debiting the account Bills Rediscounted with the Federal Reserve Bank of New York for the amount maturing. At the same time the asset account to which the maturing item was originally charged is credited, just as would be the case had the item remained in the possession of the bank and been collected.

### Pledges to Secure Public Deposits

Whenever a bank receives government funds on deposit it is required by law to furnish certain collateral as security. One form of security used for this purpose consists of notes and acceptances from the portfolio of the bank. Paper to be used for this purpose is pledged with the federal reserve bank, which acts as a trustee for safeguarding the interests both of the depositor and the depository bank. Upon sending paper to the federal reserve bank for this purpose the face amount pledged is transferred from the Bills Discounted account to an account termed "Bills Discounted to secure United States Deposits."

### Departmental Proof

At the close of the day a daily proof of entries which have arisen from the operations of the department is prepared. Mention has already been made of the fact that the debits and credits are handled in most cases by making entries for aggregates rather than by putting tickets through charging and crediting the proper account for each individual transaction. The most important journal entries for the day's operations follow.

1 Debits to the general ledger accounts, Bills Discounted Domestic, Bills Purchased, Acceptances of This Bank—Foreign, Acceptances of This Bank—Domestic, Acceptances of Other Banks, and Various Acceptances, are made for all discounts and purchases of these respective items. Figures for these charges are obtained from the totals of the corresponding columns in the offering book.

Credits are made to the above accounts for the totals of each class which have been collected. The figures for these credits are taken from the day's totals of the columns in the ticklers, after allowance has been made for unpaid items and for those which have been paid only in part.

2 The Discount Collected But Not Earned account is credited for discount deducted according to the unearned discount column in the offering book.

3 Exchange account is credited for the total amount of exchange deducted according to the exchange column of the offering book.

4 Cashier's Check account is credited for the aggregate amount of cashier's checks issued, according to the cashier's check column of the offering book.

5 Customers' accounts are credited for the proceeds of notes which they have discounted for credit, according to the columns of the offering book, and they are debited for commercial paper purchased for them.

6 The note teller is debited for the certified notes, checks, and items payable at this bank which the discount department sends to him.

To assemble these entries on the records, subsidiary proofs of the discounts made and of the collections are prepared. To facilitate this work a journal similar to the journal of the city collection department is operated. The subsidiary proofs are consolidated to form the daily proof of the department, as illustrated in Form 52. This proof is sent to the general







bookkeepers of the bank where the proper entries are made to the books of account

### Auxiliary Records

Besides the records already mentioned certain other records of a more or less subsidiary and statistical nature are kept. For the use of the cashier there is prepared a daily report giving a resume of the discounts made during the previous day. Records of each individual transaction are made under the following captions: name, amount, rate, maturity, and total amount which is under discount for the particular borrower.

Another record kept for the guidance of the officers of the bank in connection with future discounts is the statement of periodic discounts, prepared daily. This record, which is divided into two sections—one for bills discounted and one for purchased paper—shows the total amounts maturing for the day upon which the statement is issued, the following day, and for half-months for a period of three months, after which all maturities are totaled. This statement, showing as it does the exact amounts maturing for some time in the future, is a valuable memorandum to the bank's officers and enables them to tell at a glance what funds will become available for use by the bank from maturing discounts, and when.

Maturity books giving the names of the borrowers of the bank arranged in alphabetical order, with a total of the amounts under discount and the maturity date, are kept for the use of the officers in granting accommodation. These books are posted every evening, at which time maturing obligations are canceled and new ones entered.

A card file of each borrower is also maintained. This file shows the names of those who may negotiate loans and the names of those who are authorized to sign notes, etc., for each concern. It is used in passing upon notes offered for discount.



### Customers' Liability Ledgers

The most important auxiliary records are the customers' liability ledgers, illustrated in Form 53. These books do not enter into the regular accounting work of the bank, they are rather for the purpose of furnishing information as to the amounts borrowed and still outstanding against each borrower. These records are used mainly for the purpose of answering inquiries from the credit department and from the officers of the bank regarding the outstanding liability of a prospective borrower. Theoretically these books give information which prevents the bank from loaning more than its legal capacity of 10 per cent of its capital and surplus to any one customer. As a matter of fact, however, a large bank has capital and surplus sufficient to enable it to grant any reasonable line of credit without fear of overreaching the legal limits.

The customers' liability ledgers are subdivided into two groups: one showing liability under acceptances, and the other under all other classes of paper. Each group is divided into two subgroups containing bank and non-bank accounts respectively, and the records of each of these subgroups are kept in a convenient number of volumes according to an alphabetical classification. Sheets of one color are used for recording liability under purchased paper and another color for that under bills discounted.

The customers' liability ledgers contain a page or section for each customer who borrows from the bank. The usual space reserved for the heading of the account contains—besides the name, the address, and the business engaged in by the customer—the names of those having authority to borrow for the account, those having authority to sign, guarantors, if any, maximum amount under discount during the current year, and customer's liability as an indorser. As each discount is made the bookkeepers enter in this book under the name of

the borrower the date of the transaction, rate, maker, indorser, and when due. The amount of the obligation is then added to the balance already outstanding, if any, and the resultant new balance is extended in the balance column. As discounts are paid off, entries are made showing the date and the amount of payment, then the amount paid is deducted from the balance outstanding, and the new balance is extended in the balance column. Paid items are immediately ruled off in order that the observer may tell at a glance what specific items constitute the balance outstanding. From this book can be obtained such information as the amount now owing by a given borrower, maximum amount of indebtedness during a given period, number and length of times out of debt to the bank for a given period, discounts outstanding, together with their maturities, etc.

## CHAPTER XI

### FOREIGN DISCOUNTS

#### *Nature of Transactions*

A foreign discount transaction consists of an advance of funds made by the bank to the owners of foreign bills of exchange—either clean or documentary—checks, etc., payable in foreign countries, which are collectible some time in the future. This transaction resembles the foreign export collection in that the instruments dealt with are exactly the same in nature. The difference between the foreign discount and the foreign collection lies in the method in which the items are handled. In making a discount the bank becomes the owner of the instrument, paying the customer the proceeds at the time he presents the item to the bank, while in making a collection it acts as the customer's agent, paying him only after it has received the proceeds from abroad. Thus the element of credit enters into the foreign discount transaction, and in this respect this transaction is also similar to the domestic discount.

The foreign discount transaction takes one of two forms according as the item offered for discount is drawn in dollars or in foreign currency. If the offering is drawn in foreign currency, it is purchased by the bank at a flat rate and the transaction is spoken of as a "purchase" of foreign exchange. If, however, the offering is drawn in the currency of the United States, it is discounted at a given rate and the transaction is called a "discount." There is, however, no essential difference in principle between purchasing a bill drawn in foreign currency at a flat rate of exchange and in discounting a bill drawn in dollars.

### Foreign Discount Department

The work of handling a foreign discount may be divided into two phases (1) purchasing and remitting—which includes entering and approving the item offered for discount, settlement with the owner, and transmission of the item abroad for collection, and (2) making adjustments as between drawers and drawees of drafts, and attending to settlements between the bank and its foreign correspondent. It should be remarked at this point that a large part of the term of discount for a foreign item is generally consumed in sending the item abroad for collection, hence the bank is not obliged to hold such an item in portfolio until maturity, as it is in the case of a domestic discount. It remits these items abroad for collection or for rediscount immediately upon receipt, and the foreign correspondent holds them for whatever time is required.

The foreign discount department attends to the work of handling the foreign discounts of the bank. This department is so organized as to render intimate personal service to the bank's clients. Accordingly, the unit plan is in use. Each unit attends to all the business of those customers whose names fall within certain subdivisions of the alphabet. Under this plan the members of the department become intimately acquainted with the needs of the customers whom their particular unit serves, and they are therefore in a position to offer a higher degree of personal attention than would be the case under another type of organization.

### Customer's Letter of Instructions

From the time the offering is submitted to the bank until the proceeds have been received and accounted for, a customer's letter of instructions (Form 54) serves to guide the department in the particular transaction. Customers who regularly transact business through the department generally

use a standard form letter furnished by the bank. If this form is not presented with an offering the window clerk receiving the item prepares one. This letter shows the name and address of the owner, name of drawer, name and address

To The National City Bank of New York 25 WALL STREET NEW YORK, N. Y.		From <u>Star Reporting Co.</u> <u>125 Broadway</u> <u>New York</u>	
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Serial: \_\_\_\_\_  
We have your draft No. 11534 which we desire you to accept  
on 11/19/31  
Payable to cash after sight  
Term 30 days after sight  
Drawn on Guaranty Bank  
Add to Guaranty Bank  
The following documents are attached to this draft and ordered for it:

Draft		Date of Issue		Date of Maturity		Date of Payment		Date of Collection		Date of Redemption	
Original	Copy	1	2	3	4	5	6	7	8	9	10
<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>

Deliver documents against payment  
Deliver documents against acceptance  
Payable (payment) (acceptance) I this draft upon receipt of relative documents  
If paid before maturity allow value of \_\_\_\_\_ & not return for cash and collection charges on this transaction will be paid by ( )  
(Drawn)

Cable Payment  
Cable Non-payment  
Payable for Non-payment  
Cable Acceptance  
Cable Non-acceptance  
Payable for Non-acceptance  
No Provisions

Other Special Instructions  
3. Draft of paying per check enclosed  
(By name of R. R. Kennedy & Co.)

Amount at 100		Deductions		Present	
<u>1179 50</u>	<u>1179 50</u>	<u>1179 50</u>	<u>1179 50</u>	<u>1179 50</u>	<u>1179 50</u>

Serial P. 100. 1. Instructions  
☐ Cash ☒ Credit  
s/s

We have placed our initials in the space opposite the instructions which we desire you to follow  
In case of difficulty or need clarify communication with:  
Name Star Reporting Co.  
Address 125 Broadway  
who is empowered by us to make any adjustments  
necessitated with the documents.

DATE: March 22, 1931 Yours very truly Star Reporting Co.  
By John Brown  
President

FORM 54 LETTER OF INSTRUCTIONS ACCOMPANYING FOREIGN ITEM FOR DISCOUNT  
(Size 3 1/2 x 16)

of the drawee, list of documents, tenor of draft, amount of draft, instructions as to protest for non-payment or non-acceptance, instructions as to communicating by cable in case of dishonor, etc. In addition, certain information of a more or less general nature is included. It is highly desirable, for example, that the owner state whether he has an agent located in the foreign city competent to act for him in settling disputes which may arise in connection with the collection of the item.

In offering a documentary time draft for discount it is also important that the customer instruct the bank as to whether documents are to be delivered to the drawee on payment or on acceptance of the draft. In the absence of specific instructions in this matter banks are obliged to follow the varying customs prevailing in foreign countries. Among South American countries the ruling generally is that documents are deliverable upon acceptance of the bill. Among the countries of the Far East, on the other hand, documents are deliverable against payment only, irrespective of the usance of the draft. Thus the importance of having the customer indicate the method which he wishes the bank to follow is apparent.

The letter of instructions is attached to the offering through all stages of the work until the point is reached where the bookkeeping tickets and letter of transmittal are prepared and payment is made to the customer. As the offering passes through each stage any available information bearing upon how the offering is to be handled is added to the letter. When, therefore, the time arrives for preparing the tickets, the letter of transmittal, and for paying the customer, the letter gives complete directions for this work. Afterwards it is filed as an original record of the transaction.

### Window Blotter

At the outset, entry regarding the offering is made in a window blotter. This shows the name of the customer offer-



ing the discount together with the amount of the offering. The purpose of this blotter is to show whether or not possible credits for the account of any particular concern are being held. Such information is of importance in answering inquiries regarding overdrawn accounts.

### Credit Rating of Customer

The most important consideration preliminary to accepting the offering for discount is the credit rating of the customer. Customers of the bank who expect to borrow through the foreign discount department receive from the officers of the bank lines of credit which apply exclusively to these discounts. Such lines are recorded in bills registers. When an offering has been received the bills register containing the account of the customer is consulted to ascertain if the unused portion of his line of credit is adequate to care for the accommodation asked for. If such is found to be the case the offering is accepted without consulting further with the officers in charge of approving applications for accommodation.

Often, however, the line of credit arranged for by the borrower will be exhausted because of previous discounts still outstanding. Again, new or occasional customers for whom no lines of credit have been established may make application to have the bank discount foreign instruments. In either case an offering ticket is submitted to the officers in charge of the applicant's territory for approval in the same way as for the domestic discount.

### List Book

In order to furnish information to the management regarding the transactions, each approved offering is entered alphabetically in the list book. The information shown consists of name of customer for whom discount was made, the country of the payee, and the amount of the draft. At the end of the

day lists are prepared from this book and submitted to the officers

### Number Register

To aid in recovering items which may be mislaid and to assist in carrying on correspondence with foreign collecting agents, each discount item has a serial identification number. The proper number is assigned to each offering as soon as it is approved. This number is stamped upon each instrument and document composing the offering—draft, shipping documents, certificate of insurance, customer's letter, etc. The numbered offerings are entered consecutively in a bound index book, and on a line with a given number is listed the name of the seller and the amount of the item—in dollars or in foreign currency.

### Examination of Documents

After an offering has been approved, the unit which regularly cares for the business of that particular customer takes charge of it. Within the unit the transaction first comes to the attention of the documentary clerks whose function it is to make a complete examination of the offering and to authorize payment only when everything is in proper order for effecting collection abroad. In theory, at least, the examination of documents by the discount department needs to be more thorough than that to which similar documents are subjected by the foreign collection export department, because the discounted item becomes the property of the bank, and the accompanying documents, carrying as they do title to the shipment, give the bank additional security, while the documents attached to the collection item, so far as the bank is concerned, carry with them no such significance.

In the examination process the draft itself receives first consideration. The examiner sees that it is properly drawn

and properly signed, that the date, the filling, and the amount are in order, and that the latter two agree with the amount of the invoice. It must also be noted whether any charges which have been added to the invoice amount of the shipment to make up the face of the draft are adequately explained and whether they are handled in a manner conforming to the usage which obtains in the country of the drawee.

The merchandise invoice is next compared with the bill of lading with respect to the mark and description of the merchandise. The examiner sees that the two agree exactly on these points. He next examines closely the bill of lading itself. First of all he determines whether the full number of copies certified as having been drawn up by the steamship company, are in his possession. This matter is of vital importance, since a missing document which conveyed title to the goods would expose the bank to the possibility of loss should it fall into the hands of an unscrupulous person. The examiner must also see that all copies are properly made out, that they properly describe the merchandise, and, furthermore, that they are indorsed to the bank and that the signatures appearing on the indorsements are authentic.

Insurance certificates furnish the bank protection in case the goods are damaged or lost in transit. They are accordingly subjected to a careful examination along with the other documents. The examiner sees that they are correctly executed, signed, and, if they are made out to the shipper's order, that they are indorsed to the bank. The adequacy of the insurance both as to kind and amount is important. As to the face of the policy, it is the custom to require 10 per cent in excess of the invoiced value of the shipment. As to the kind of insurance, it is of paramount importance that the policy cover all risks for the entire journey from the shipper to the consignee.

Irregularity with respect to any of the considerations

enumerated above may delay or prevent payment abroad, carrying with it considerable expense and delay in effecting final settlement. Should any defect be discovered the bank communicates with the customer and has him make the necessary corrections before it proceeds further with the transaction.

### **Methods of Negotiating Foreign Bills**

From the standpoint of the customer there are three methods which may be used in negotiating foreign bills: (1) the discount, (2) the purchase, (3) and the advance against collections. In making a straight discount or a purchase the bank pays the proceeds to the customer at the time the transaction is received, just as it does in the case of a domestic discount. A transaction handled as an advance against a collection is similar to a loan in the domestic division. Such a transaction may be handled in one of two ways: net, or subject to adjustment. If it is handled net, the bank advances the customer the face of the bill and collects the entire amount of it, plus all charges from the drawee at the other end, or from the customer upon receipt of funds and advice from abroad. The subject to adjustment transaction, on the other hand, is made upon a part-payment basis. In this case the bank advances a percentage of the face amount of the item to the customer. It is understood that after the transaction has been completed, that is, after the item has been collected from the foreign customer, the bank will settle with the customer by deducting its charges and remitting the balance, if any, due to him.

### **Discount Rates**

The rate charged by the bank may be either a foreign exchange rate or it may be a discount rate, as has already been noted. Foreign currency bills are always purchased, while dollar items are handled on a discount basis. In case the

bill is purchased, the rate takes the form of an exchange rate which is fixed by the traders of the bank. This consists of a basic rate determined by the state of the market, to which are added the necessary expenses of the bank for interest, commission, and bill stamps.

For example, let it be supposed a customer offers for discount a £5,000, 90-day draft drawn on London and the traders quote a rate of \$4 69. The calculation would be as follows:

Face of Draft	=	£5,000
Conversion Rate £1	=	4 69

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Proceeds for Customer = \$23,450 00

In case the bill is discounted, the rate is a discount rate. The discount rate is made up of four parts:

1. Interest at the current rate for the time the bank expects to be out of funds.
2. The domestic bank's commission, that is, its usual charge of  $\frac{1}{8}$  per cent for collecting the item, which corresponds with the commission charge mentioned in connection with the collection of foreign items.
3. The charge of the foreign correspondent for commission, which is also the same as that mentioned in connection with the work of the foreign collection export department.
4. The charge for bill stamps, which will be made under the revenue laws of the country of destination.

These items are combined into a flat rate at which discount is deducted from the face of the item.

Discount charges are usually borne by the owner, though sometimes by the drawee. There is no definite rule, the entire proceeding depends upon the contract between the drawer and the drawee. When the contract provides that the drawee is to bear all interest and banking charges, the better practice is for the drawer to include such charges in his merchandise

invoice and to draw his draft for the full amount. The bank may then discount or purchase such an item on a straight basis. Yet the drawee bears the expense since the charges are included in the face of the draft.

If the charges are not included in the invoice and in the face of the draft and the drawee is to bear the costs, the bank adds the charges to the face of the draft in red ink. It is not illegal to indicate upon the face of the draft that interest and collection charges are to be paid by the drawee, but were the drawee to offer in settlement merely the amount of the bill as drawn by the drawer, disregarding all notations in cover of interest and collection charges, in most countries the collecting bank would be obliged to accept the offer so made by the drawee. Indeed, the collecting bank would be powerless to protest upon the ground that the drawee refused to pay the additional charges, and the drawee could compel surrender of the draft and documents upon his offering the amount of the draft as drawn by the drawer. Should the exporter disregard this requirement of foreign law, the endeavor to collect such additional charges may not only cause unpleasant relations between the collecting bank and the foreign customer of the exporter, but at times may necessitate considerable delay and cable expense.

While in the majority of cases it is advisable that the drawer include in his merchandise invoice and corresponding draft the cost of interest and banking charges, custom dictates in the case of drafts drawn on far eastern countries, such as China, Japan, India, Straits Settlements, Philippine Islands, etc., as well as in the case of drafts drawn on Australia and the lesser British possessions, that such charges be not included in the draft but that the discounting bank be directed to collect them from the drawee over and above the face amount of the draft. In any case the procedure to be followed is beset by technicalities, and the bank encourages the exporter, in the

absence of explicit instructions from his customer abroad, to communicate with it before drawing up his invoice and draft.

### Tickets and Remittance Letters

After the offering has been accepted and the proceeds calculated, the necessary tickets, advices, and remittance letters are prepared. To save time and effort, these various instruments are prepared at one operation. Six copies of a sheet consisting of a letter and an attached ticket stub are drawn up. The first copy constitutes a complete record of the transaction and is retained as an office copy. The letter sections of the second and third copies constitute original and duplicate remittance letters to be sent to the foreign collecting bank. The ticket section of the second copy serves as a charge ticket covering the acquirement of the asset by the bank. The ticket section of the third copy serves as a credit ticket covering the settlement made with the owner of the item.

The letter section of the fourth copy contains material for making the proper entry in the bills registers, while the ticket section of this copy serves as a credit ticket covering the discount charges, or funds retained from transactions handled on a subject-to-adjustment basis. The letter section of the fifth copy of this sheet is sent to the credit department where it is used as a basis for soliciting new business. The ticket section of this copy constitutes an advice which is sent to the customer of the bank at the time of accepting the offering. Its purpose is to notify him that his offering has been accepted for discount and it states that his account has been credited, or the ticket is accompanied by a cashier's check for the proceeds, according to the customer's instructions. The sixth copy of this sheet is the auditors' copy. It is attached to the customer's letter of instructions and the two are used by the auditors in making their daily audit of the work of the department.

### Accounts Charged for Item Received

The debit covering the acquirement of the asset by the bank is made either to the Bills Discounted Foreign account, or to the Due from Foreign Banks account of the bank to which the item is to be remitted for collection. Foreign currency items other than those drawn on the colonies of European nations are charged directly to the accounts of the foreign banks which are to effect collection. All dollar items are debited at face value to the Bills Discounted Foreign account. To this account there are also charged temporarily all foreign currency items drawn on European colonies. The duplicates of these colonial drafts are sent to London, Paris, Amsterdam, etc., to be rediscounted and the proceeds deposited with the bank's correspondents located in these cities. After the rediscount has been effected and the bank has received information regarding the amount of proceeds placed to its credit in Europe, entries are made to withdraw the rediscount from the Bills Discounted account and to charge the proper amounts to discount paid abroad and the proceeds to the account of the foreign bank.

The offsets to the charges just mentioned consist of one credit covering the proceeds of the discount and another covering the amount retained by the bank. The credit covering the proceeds is made to the customer's deposit account or to the Cashier's Check account according to his instructions. The credit for the amount retained is either to the Discount account or to the Funds Retained account. In case the discount has been handled on a straight basis, the bank will have retained only its discount charges, hence credit for this amount is made to the Discount account. In case the bank has handled the discount on a subject-to-adjustment basis a larger proportion of the face value of the draft will have been retained. This amount is credited to an account termed "Funds Retained," pending final settlement.



### Remittances Abroad

In general the remittance of discounted items to foreign correspondents and branches for collection is the same as the remittance of items for collection through the foreign collection export department, but since the bank is the owner of discounted items and may accordingly use the proceeds as it sees fit, there are some differences. The bank may convert the item from one currency to another before remitting it, and it may forward the item for collection and remittance, for collection and credit, for deposit, if a sight item, or for discount and credit.

In case the customer desires the bank to collect charges in whole or in part from the drawee, the following information is stamped on the remittance letter

Kindly collect this draft, plus our  
charge of . . . together  
with interest at . . . per cent  
from date of draft until approxi-  
mate arrival of proceeds in New  
York Stamps and all your charges  
are to be collected from the drawee

### Bills Drawn upon British Colonies

Drafts drawn in foreign currency are transmitted to foreign correspondents to be credited to the foreign currency account of the American bank maintained with these foreign banks. Items drawn in pounds sterling upon drawees located in the British colonies are generally rediscounted in the London market. The original items are despatched to the British branch bank located in the colonial city of which the drawee is a resident. The remittance letter and the drafts themselves are stamped with the following information

Payable with exchange and English  
and Colonial Stamps at the current  
rate for negotiating bills in Lon-  
don on the colonies

Duplicate draft and documents have  
been forwarded to your London  
office for negotiation and payment  
of proceeds to the (insert name) in  
London.

The duplicate draft and documents are forwarded to the London office of the colonial bank to which the original has been despatched. These duplicates contain the following stamps:

Payable with exchange and English and Colonial Stamps at the current rate for negotiating bills in London on the colonies

Original draft and documents have been forwarded to your (city in colony) office. Please negotiate this draft and pay proceeds to the (insert name) in London, plus your usual commission, for the credit of our account.

In this manner the account of the American bank with the London correspondents receives immediate credit for the face amount of the remittance because of the fact that the draft is made payable at the current rate for negotiating bills in London on the colonies, together with exchange and all stamp charges. The bank is therefore out of funds merely for the time required for the voyage to London, and the drawee meets all charges.

### Time Sterling Bills

Time sterling drafts, whether clean or documentary, are sent to the London correspondent of the bank with instructions that the same be discounted immediately in the London discount market and the net proceeds placed to the credit of the American bank, or that the item be held until maturity subject to further instructions. These further instructions are issued by the traders of the bank who are quite likely to have the item discounted at any time before maturity when the London discount rate becomes favorable. An item held pending instruction as to rediscount is said to be held in "Depot" account.

### Dollar Items

Dollar items may be handled in one of two ways: (1) they may be converted immediately into foreign currency at the

prevailing rate, or (2) they may be forwarded for collection as dollar items with the request that dollars be remitted from abroad

The first method is used only for bills drawn on Australia and other British colonies of the Far East. Irrespective of their tenor the bank converts such drafts into sterling at the prevailing check rate on London. There is a market in London for bills drawn on the English colonies and especially for bills drawn on Australia, so that a bill of a given usance will be bought and sold at a current rate of exchange, which rate will take into consideration the length of time that the London bank will be without funds. In addition to this exchange the Australian drawee will be obliged to pay to the collecting bank the cost of English and colonial stamps together with such collection charges as the London bank may exact. There is no such market for Australian bills in New York.

Furthermore, while every Australian bank necessarily carries a balance in London, very few Australian banks carry dollar balances in New York. It is obvious, therefore, that London exchange is more readily obtainable in Australia than New York exchange, and the premium or exchange to be paid for these two classes of money varies correspondingly. In other words, barring violent fluctuations, Australians invariably prefer to settle their bills in sterling. The drawer of a bill in New York, on the other hand, is not particularly interested as to whether the Australian settles in dollars or in sterling. The discounting bank in New York will pay the drawer the face amount of his draft drawn in dollars and the drawer is entirely out of the transaction unless the bill is dishonored.

### Other European Colonial Bills

Bills drawn in francs, guilders, and marks upon drawees located in colonial territories of France, Holland, and Germany

are handled in a similar manner to the treatment given a British colonial item. The original drafts and documents are forwarded direct to the collecting banks in the colonies, while the duplicate drafts are rediscounted in Paris, Amsterdam, or Berlin.

### Other Dollar Drafts

All dollar bills drawn on points other than the British colonies just enumerated are payable at the collecting bank's selling rate for sight drafts on New York. This simply means that the drawee is obliged to pay to the collecting bank the same number of pesos, francs, lire, or sterling, as he would be obliged to pay were he to purchase a dollar draft on New York for the exact amount of the dollar bill drawn against him.

In countries where the American dollar does not pass as legal tender, obviously such a notation or instruction is unnecessary. A drawee has no choice about the matter. He must offer a sufficient amount of his own currency as determined by the rate of exchange applicable on the date of payment to purchase the necessary amount of dollars to retire the bill drawn against him.

The situation is different, however, in countries where the United States dollar passes as legal tender. This refers in particular to Cuba, Porto Rico, Panama, and Santo Domingo. Unless a notation is made on the draft, or the instructions transmitted to the collecting bank provide that the dollar bill is payable at the collecting bank's selling rate for sight drafts on New York, the drawee may offer in settlement of the dollar draft drawn against him actual United States currency equivalent to the amount of the draft. Were the collecting bank to accept such settlement it would be obliged to transmit the dollars thus collected to New York, and immediately the matter of loss of interest would enter into the transaction.

The collecting bank is not satisfied to hold the dollars so received in its vaults and to instruct the New York bank to debit its dollar account carried with it, for the reason that the collecting bank is able at all times to sell its dollar balances carried with the New York bank at a premium. Therefore, for the protection of the collecting bank, such a notation is stamped on all dollar drafts payable in these countries.

In the case of bills drawn on Canada it is also imperative that the draft makes it perfectly plain as to whether payment is to be made in United States dollars or in Canadian dollars. Payment in dollars is specified by indicating on the face of the draft that the same is payable at the collecting bank's selling rate for sight drafts on New York, as mentioned in the preceding discussion.

The remittance letter for dollar drafts, unless converted, and the drafts themselves are always stamped "Payable by Demand Draft on New York," and the bank requires this demand draft to be an approved banker's check. This stamp gives the drawee the option of paying the obligation at the rate of exchange calculated by the correspondent, or in the event that he feels that the drawee is being overcharged, he may buy a demand draft on New York in the open market and tender such a draft in payment.

### Settlement Required from Collecting Agents

In choosing its collecting agents the bank naturally favors those institutions which carry dollar accounts with it. At times it becomes necessary, however, for it to remit items for collection to institutions which have no accounts with it. The general instructions accompanying all remittance letters provide for this contingency by giving the collecting bank option of making settlement on one of two plans. First, the collecting bank may collect the draft at such a rate that the New York bank may, upon receipt of the relative advices

of payment, debit the Dollar account of the foreign collecting bank for the full amount of the collection. Second, in the event that the collecting bank does not carry an account with the New York bank it may remit in settlement an approved banker's check on New York for the required amount.

### Settlements Between Banks

After items have been paid for and transmitted to the foreign bank for collection there still remains the work of making adjustments of dishonored items, of smoothing out differences between drawer and drawee, and of effecting settlement with the foreign correspondent. If the transaction is consummated without impediment, the foreign correspondent sends an advice of acceptance after the item has been accepted and an advice of payment after the item has been paid. The foreign bank asks that its account be debited for the net amount collected or it sends a remittance which it asks the bank to accept. The New York bank complies with this request and it debits its Discount account for the charges made abroad and credits the Bills Discounted Foreign account for the amount of the bill collected. The item is then stamped out of the bills discounted ledger. There are, however, innumerable variations from the ideal transaction. In fact the majority of the transactions are exceptional in some way and a very large part of the personnel of the foreign discount department is devoted to handling correspondence arising from irregularities in or dishonor of items.

### Adjustments

For guidance in smoothing out the difficulties which may arise in the collection of items abroad, recourse is had chiefly to the files and the bills registers which have already been mentioned. Upon receiving notice that an item needs adjustment the correspondence clerk of the unit obtains from the

files all information regarding the transaction and makes a careful investigation. Since the bank has taken the discount with recourse to the owner he is immediately communicated with in order to obtain his instructions regarding adjustment of the transaction. A résumé of each transaction pending settlement is entered in a tickler which serves to call the item regularly to attention until settlement is effected.

There are various types of adjustments which the bank is called upon to make. Considering first adjustments of the face of the item, the situation often arises wherein the foreign drawee refuses to pay the amount of the draft or to accept it, on the grounds that the shipment of goods is not satisfactory, that the merchandise is not as contracted for, etc. In a case of this sort the two banks act as a medium for adjusting disputes between the two parties and they often secure adjustment in the form of a rebate. Whenever the customer has a competent agent abroad adjustments are facilitated by having the foreign collecting bank deal with the agent direct.

Upon advice from the foreign correspondent that the agent of the customer has allowed a rebate, or upon direct advice from the customer to that effect, the amount of the rebate is immediately taken out of the Bills Discounted Foreign account and charged to a special account termed "Accounts Receivable—Foreign Discount." To this charge for rebate are added such expenses as cable fees and others incurred in effecting the adjustment. The customer settles such charges by sending a remittance which is credited to his account in the accounts receivable—foreign discount ledger, or by advising the bank to debit his deposit account.

### Transactions Subject to Adjustment

Transactions which the bank has taken subject to adjustment require special treatment after collection abroad is

effected. It will be recalled that the bank advances the customer only a part of the proceeds of his discount, and credits the balance to the Funds Retained account. When the bank receives advice from a correspondent that an item of this sort has been collected, it is in a position to calculate its charges accurately and to deliver the remainder of the funds retained to the owner. Entry covering such transaction is made by debiting the Funds Retained account for the total amount retained in connection with this particular discount, and crediting the Discount account for the amount of discount and the customer's deposit account or the Cashier's Check account for the amount returned to the customer.

#### Adjustment of Dishonored Items

In a few cases the particular controversy between the drawer and the drawee assures the bank that the item will not be taken care of as anticipated by it when the discount was first negotiated. When payment of an item of this sort has been delayed the transaction is in fact a rediscount and the matter of carrying the transaction further is referred to the management of the bank for approval. In this case the transaction receives the same consideration as it did at the time of the original offering. Often the management does not deem it good policy to await reimbursement upon an advanced maturity date. In other cases the item is dishonored outright. In either event the bank requests the drawer to send a check for the amount advanced to him less any unearned interest. At the customer's request the item is then entered on a collection basis if there is any hope that it will be ultimately collected. In case the drawer has been allowed unearned interest the amount of the allowance is charged to Discount account. Pending receipt of a check from the drawer in reimbursement of such an item, the asset charge is transferred from Bills Discounted—Foreign, to Accounts Receiv-



able—Foreign Discount After the customer's reimbursement is received tickets are prepared which close the item out of this account and the transaction is sent to the foreign collection export department, if the customer desires the bank to continue with it. After the proper entry has been made in the bills register and bills discounted books the foreign discount department is no longer concerned with the transaction.

### Notice of Collection for Customer

Although the discount item is its own property, the bank nevertheless pursues the policy of sending notice to the owner of the item, both when the item is accepted abroad, if it is a time item, and when collection has been effected. The purpose of this notice is to enable the drawer to know at the earliest possible moment whether or not his drafts are being duly honored, so that in the event he may have ready a second shipment to the drawee he may take immediate steps to forward it. International business is much like domestic business and it is conducted largely upon the credit of the buyer, but sellers are not overanxious to increase the amount of their credits outstanding when the buyer is thousands of miles distant. Much delay to the customer's business, however, is avoided through this simple service on the part of the bank in sending notice of acceptance and of payment to him. At the time of receiving and sending these advices of acceptance and payment the bookkeepers in charge of the bills discounted ledgers enter these facts in the proper places on the books.

### The Books of Record

Two important books of record are kept in the foreign discount department, the bills registers, and the bills discounted ledgers.

### Bills Registers

The bills registers, a sheet of which is illustrated in Form 55, serve a variety of functions. In the first place they are used to indicate the contingent liabilities of borrowers under foreign bills discounted. In the second place they contain a detailed record of each transaction. They are therefore used for reference whenever it becomes necessary to refer to any transaction. In the third place these registers serve as a tickler for bringing to attention items which are retarded in the collection process and which should be followed up.

A separate volume of the bills registers is kept by each unit and there is a separate space in this register for each customer whose business is handled by this unit. When a transaction first comes to the attention of the unit, entry is made in the bills register to show the date the item is offered for discount, number assigned to the item, customer's number or letter date, the name and address of the drawee, the nature of the merchandise, and the tenor of the draft. Entry showing the face value of the draft is also made in the "Debit Amount" column of the register. Upon the following morning the bookkeeper of the unit receives a memorandum in the form of a copy of the remittance letter which shows that the item has been mailed. From this copy entry showing the name of the foreign collecting bank is made in the "Remitted To" column. This method of making the entry acts as a check that every item entered in the register has been actually mailed for collection.

Upon the morning following the discounting of an item the general bookkeepers of the bank return to the proper unit of the foreign discount department the ticket debiting Bills Discounted—Foreign, and from this ticket the unit head enters the rate of discount and the amount of discount in the proper spaces in his bills register. The method of making

these entries serves as a check that every item entered in the register has actually been paid for and that the proper bookkeeping tickets have gone through the machinery of the bank

At this time the unit head also indicates under the proper

BOUGHT OF <u>Smith &amp; Jones</u> ADDRESS <u>New York City</u> ENTERED							
DATE	NUMBER	CUSTOMER'S NO. OR DEDUCTION	DRAWEE AND ADDRESS	PAID TO	CODER	TENDER	
3/21/21	626407	275	A B Hadley Buenos Aires, Arg.	M C B B A Arg	Cotton Goods	90 d	
	626301	274	James H Peterson & Co Melbourne, Aust	Emp Scot & Aust Bk Ltd Melbourne & London	Cotton Pieces Goods	30 d	
	626200	273	Garcia & Co Melbourne, Aust	"	"	30 d	
5/21/21	626508	777	J C Moore & Co Paris, London	Long to commission of discount de Paris Melbourne Aug 1st to commission of discount for the Paris, London	"	60 d	
5/28/21	627896	279	J H Marston Adelaide	Bk of Australasia Ltd Adelaide & London	Cotton Goods	30	
5/28/21	627896	278	Chapman & Watson Co Sydney, Australia	Bk of Australasia Ltd Sydney & London	"	60 d	
6/7/21	629301	280	B B Price Bombay, India	J C B Bombay, India	"	60 d	
6/10/21	630439	281	H H West & Co Rio, Brazil	M C B Rio de Janeiro, Bra	"	90 d	

Form 55. Bills

heading "Approximate Due Date" the approximate date when the item is due abroad. When this approximate due date arrives, in the absence of advices to the contrary, the unit head fills in under the heading "Credit Amount" the face amount of the draft, thus reducing the contingent liability of the customer by the amount of the draft now presumably

paid The balance under discount, if any, is extended in a column headed "Running" The purpose of this column is to give the observer at a glance the contingent liability of the customer If after an item has been credited out of the customer's contingent liability on the presumption that it has

LINE <u>50,000.00</u> N C B - N Y											
RATE	AMOUNT	FOREIGN CURRENCY	DEBIT AMOUNT	DATE	DATE	AMOUNT	AMOUNT	AMOUNT	AMOUNT	AMOUNT	AMOUNT
3 1/4	15 25		562 60	9/20					11/18		
3 50 1/2		£ 417 1/4	1,517 81	8/6					7/21		
3 80 1/2		£ 204 1/2	779 80	8/6					9/21		
3 76 1/2		£ 211 1/4	795 26	8/7					9/9	Enter 4/7 accepted	
3 90 1/4		£ 111 1/2	436 93	7/12					9/10		
3 57 1/2		£ 512 1/4	1,934 95	9/10					11/1		
net			3,363 42	9/22					11/21		
3 3/8	11 90		350 35	10/10					12/5		

Register (Size 22 x 17)

been paid abroad, the bank receives an advice to the effect that the item has not been paid, the amount of the draft is re-entered in the debit column of the register thereby restoring the amount of the customer's contingent liability.

The last three columns of the bills register constitutes a tickler for items which should have attention. In a column

headed "Due New York" there is entered the approximate date when the relative advice of payment from abroad should arrive in New York. A column headed "Out B D Ledger" is used for recording the date upon which advices are received from abroad. Items which should have been heard from are readily brought to attention by means of the lack of an entry

BILLS FOR									
DATE	FOR THE CURRENT	PAID TO	RECEIVED TO	TERM	RATE	AMOUNT	DATE	RECEIVED	DATE
12/24/20		John Doe & Company	Pagos de Barranquilla	60/4	2 1/2	3	24	4/12	
"		J. H. White	Pagos de Barranquilla	100/4	3 1/2	3	52	4/19	
"		S. D. Smith & Co	" del Peru	100/4	3	79	26		
12/27/20		W. B. Gorton & Co	Com. P. de Alfama	100/4	4 1/2	6	24	4/13	
"		P. V. Hartley & Sons	P. B. de Panama	100/4	3 1/2	1	22		
"		" " " "	" " " "	100/4	4 1/2	4	24	4/19	
"		" " " "	Pagos del	100/4	4 1/2	"	"	4/17	
"		B. C. Kierman & Co	del Peru	100/4	"	"	"	4/13	
"		H. S. Dixon	Pagos Justo	100/4	"	"	"	3/22	
"		R. H. Mears & Co	" " "	100/4	3 1/2	9	03	4/22	
12/27/20		J. C. Watson & Co	" Com. de Panama	100/4	4 1/2	"	"	4/16	
12/27/20		G. S. Burns & Co	" del Peru	100/4	2 1/2	2	24		

Form 56 Bills Discounted

appearing in the "Out B. D. Ledger" column on the approximate date indicated in the corresponding "Due New York" column. Items of this sort are followed up by the correspondence clerks of the unit. Indication of the date upon which tracing operations commence is made in the "Dishonored or Tracing and Date" column of the register.

### The Bills Discounted Ledgers

The bills discounted ledgers (Form 56) are the departmental subsidiary ledgers containing in detail under various subdivisions the figures and attending explanations covering

the charges and credits to the account on the general books called "Bills Discounted—Foreign." In this respect the account Bills Discounted—Foreign, controls the bills discounted ledgers and the sum of all the outstanding items on the ledgers at any one time should equal the debit balance of the Bills Discounted—Foreign account

DISCOUNTED EIGN									
DATE CREDITED AMOUNT	DATE DEBITED AMOUNT	DATE CREDITED AMOUNT	NUMBER	DATE DEBITED A. T.	AMOUNT	DATE D. L.	DATE D. L.	REMARKS	DEBITED
4/16 4/15			160 252		175 01	July 8 1921		<i>subject to adjustment</i>	
4/15 4/16			54		160 50				
			56		625 01	July 12 1921			
4/16 4/17			211		147 61	July 14, 1921			
			221		34	July 8 1921			
4/20 4/21			213		113 45				
4/21 4/22			262		111 45	July 12 1921			
4/23 4/24			266		1,567 75	July 8 1921			
4/26 4/27			274		930 29				
4/27 4/28			326		219 05				
4/28 4/29			184		252 29	July 22 1921			
4/29 4/30			357		89 51				

Ledger, (Size 20 x 18½)

In general these ledgers serve two purposes. In the first place they are used to record the numerous details relating to the remittance abroad and collection of an item from the time the transaction is first accepted and placed on the books of the bank until the settlement funds are received from the collecting bank in liquidation, or until the item is removed from the books of the department owing to dishonor abroad or transfer to the collection department. In the second place they serve to show, by divisions and banks, items in the hands of foreign collecting correspondents still unpaid, and the total of such items substantiate the debit balance to the Bills Dis-

counted—Foreign account In connection with the above two uses they constitute a ready reference for information concerning any items discounted or purchased and charged to Bills Discounted—Foreign

The bills discounted ledgers are divided into four general subdivisions and items are entered under these subdivisions according to the collecting correspondent bank, its locality, and the nature of the items In the first division there are included for entry all items collectible through branches of the New York bank, each branch being allotted a separate section. In the second division, the foreign currency ledger, are included all foreign currency items drawn on European colonial territory, in which case, it will be remembered, the duplicate drafts are negotiated in Europe In the third division, or "South American—various" ledger, are entered all items drawn on South American territory not collectible through branches of the home office The fourth division, or dollar ledger, handles all dollar items drawn on other than South American territory

The preliminary entries give the date, the drawer, the collecting bank remitted to, the tenor of the draft, the discount amount, the number, and the amount, these are entered from the debit ticket, charging Bills Discounted—Foreign in columns provided, in the same manner that these details are entered in the bills registers Every day a large volume of mail is received from the various collecting correspondents This includes advices of acceptances, settlement statements, and advices of dishonor. This information is brought to the attention of the bookkeepers, appropriate entries are made in the bills discounted ledgers, and other necessary steps are instituted in the liquidation of items

Upon advice from abroad that an item has been accepted, entry is immediately made under the "Actual Date of Maturity" column indicating the date when the item is due abroad Then, allowing for time to transmit the advice of payment

from abroad, entry is made under the "Due Date New York" column. The customer is advised of the acceptance of the item and this fact is also noted in a column in the ledger. When an item is paid entries are made in accordance under the "Date Letter Payment" and "Advise Customer Payment" columns, and when the ticket crediting the account Bills Discounted—Foreign comes back from the general bookkeepers, the item is stamped out of the "Out B D" column and the value date of the remittance from abroad is entered in its proper column. In case items are dishonored or taken out of Bills Discounted—Foreign for some other reason, appropriate remarks are noted in a provided column and the items are stamped out of the ledgers.



## CHAPTER XII

### LOANS

#### Characteristics of Loans

A second form of bank investment is the loan. A loan in the banking sense may be defined as an advance of funds, generally in the form of bank credit, made with the understanding that the borrower is to pay the interest on his loan either at stated intervals or at the time of maturity of his obligation. The principal difference between a loan and a discount is that in making a discount the bank deducts its charge at the time the accommodation is negotiated, while in making a loan it collects this charge at a later date. Again, the discount is necessarily payable at a definite time, while the loan is quite frequently payable on demand. In practice generally there is also a difference between the loan and the domestic discount in the matter of security. The term "loan" in almost all cases signifies a secured loan, while the term "discount," in the domestic sense, quite generally signifies an unsecured one.<sup>1</sup>

#### Classification of Loans

With respect to security there are four main classes of loans:

- 1 Loans secured by stocks and by bonds as collateral
- 2 Merchandise loans.
- 3 Loans secured by receivables
- 4 Advances made upon arrival drafts

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<sup>1</sup>See page 258, text and footnote

### Loans Secured by Stocks and Bonds

As the term indicates, loans secured by stocks and bonds consist of advances made to borrowers who have secured the advance by pledging stocks and bonds with the bank as collateral. This class of loans may be subdivided into two classes (1) the stock exchange loan, and (2) the non-stock exchange loan.

Distinction between stock exchange and non-stock exchange loans is made primarily because of differences in the method of handling the two classes rather than because of differences in essential characteristics. There has sprung up in New York certain peculiar customs and unwritten rules which to a considerable extent govern the procedure between borrowers and lenders on the stock exchange board and give this class of loans a degree of uniqueness. In keeping with this fact, those of the bank's loans which are placed according to stock exchange procedure are termed "stock exchange loans" in this study, while those made upon stock and bond collateral, but not made according to stock exchange procedure, are termed "non-stock exchange loans."

### Merchandise Loans

Merchandise loans are those made upon the security of warehouse receipts, bills of lading, and other documents covering commodities. These loans are commonly met with in financing the manufacture and marketing of the great staples, such as wheat, cotton, meat, etc. So well-nigh perfect is this type of loan in its operation that by changing the collateral successively from bills of lading to trust receipts and from either of these to warehouse receipts, it is often the case that practically the same loan covers the progress of raw material from the primary market through the mill and in the retail market, the loan being paid off from the proceeds of retail sales.

### Loans Made upon Receivables

A form of loan which is used chiefly in dealing with correspondent banks is the loan secured by receivables. In borrowing under this plan the correspondent secures the lending bank by pledging certain of the notes, or receivables, which it has discounted for its customers.

### Loans Made upon Arrival Drafts

Advances upon arrival drafts are loans made upon the security of drafts to which are attached bills of lading covering shipments of goods. These are generally short-time advances made to a consignor of merchandise to bridge the interval of time during which goods are in transit. These transactions occur in a variety of forms, but two of these forms in particular are worthy of note.

The first type of loan made on arrival drafts occurs in connection with the shipment of goods to New York City. A transaction of this sort is quite frequently financed by the seller's drawing a draft accompanied by shipping documents upon the purchaser in New York City. The tenor of this draft is such that it is payable upon the arrival of the goods at destination and the shipping documents are to be released to the consignee upon payment. The draft is then forwarded to the bank in New York City, and the bank presents it to the drawee, obtaining his assurance that payment will be forthcoming upon arrival of the goods. Upon the strength of this promise, secured by a lien upon the shipment afforded by the shipping documents and by the credit rating of the shipper, the bank advances funds to the latter, charging him at the current rate of interest and reimbursing itself for the amount of the loan when it has collected the draft.

A second important use of the advance against arrival drafts occurs in the case of shipping goods from New York City, for example, to some other city. In an instance of

this sort the shipper draws a draft accompanied by shipping documents in the ordinary way, and he forwards them by mail or delivers them to the New York bank. The bank examines the documents and if they are in order the loan against them is made for the customer, and the draft together with the documents is sent to the bank's correspondent in the city to which the goods have been shipped. When in due course of time the goods arrive and the draft is met by the consignee, funds are forwarded to the New York bank by the correspondent. The New York bank reimburses itself for the funds advanced and after deducting the interest, places whatever balance there may be to the credit of the customer's account.

### Classification of Loans According to Time

According to time to run, loans may be classified as demand, time, and day loans. The time loan is made at a fixed rate of interest and for a definite time, 30, 60, and 90 days, and 6 months are common terms. Demand loans, on the other hand, are payable at the option of either the borrower or the lender, and the rate of interest charged may fluctuate with the market.

A common type of demand loan is the demand street, or call, loan. Such loans are made strictly in accordance with the usages of the New York Stock Exchange. They are generally negotiated through money brokers who are members of the exchange. The borrowers likewise are members of that organization.

The day loan is made for the purpose of supplying the temporary needs of stock brokers. Brokers who have made arrangements to use this form of borrowing keep lodged with the loan department certain approved stocks and bonds. With these securities the broker executes a loan contract, either verbally or written, whereby he agrees that the securities are

to be held by the bank for the purpose of securing any day loan he may arrange for. Should such a broker need more funds than he has to his credit at the bank, he makes an arrangement, on the security of the collateral which the bank holds, to draw a stipulated amount for use during the day. At the close of his day, and before the bank closes, he restores his balance, thereby closing out the loan. Since such a loan does not continue for one whole day no interest is charged.

### Classification for Accounting Purposes

The foregoing classification of loans has been given to bring out the varied characteristics of these advances. In the work of the bank the classification for accounting purposes is somewhat different. This classification is as follows:

- 1 Demand street, which includes all call loans made to brokers who are members of the New York Stock Exchange
- 2 Demand merchandise, which includes demand loans made upon warehouse receipts and bills of lading
- 3 Demand loans, which includes demand loans other than those included in demand street and demand merchandise loans
- 4 Time merchandise, which includes all time loans on bills of lading, warehouse receipts, etc.
- 5 Time loans, which includes all time loans with the exception of those made on merchandise
- 6 Day loans
- 7 Advances on arrival drafts

### Functions of Loan Department

The work of caring for loans is performed by the loan department. This work consists of

1. Examining and accepting the collateral.
2. Watching margins.

3. Attending to collateral substitutions
4. Computing and collecting interest
5. Collecting loans as they mature or are called by the bank

For convenience the loan department also cares for certain discounts secured by the type of collateral which it is better equipped to care for than is the discount department

In addition to attending to loaning the bank's own funds the loan department cares for the details of one of the most valuable gratuitous services which the bank offers to its customers, viz, loaning their surplus funds for them on call to stock exchange brokers. Call loans constitute a desirable investment for a portion of a bank's temporarily inactive funds because these loans are readily convertible into cash. Stock exchanges, however, are not directly accessible to banks, excepting those located in a few of the large cities of the country. Of the few stock exchanges in the United States, the New York Exchange is by far the largest and it is the only one which can absorb funds offered in almost unlimited amount. Out-of-town banks therefore make call loans to members of the New York Stock Exchange through their New York City correspondent. The correspondent loans the funds in the usual way and it charges the customer's account for the amount involved. When the loan is paid off it credits his account for the face and the interest. The bank which loans the funds usually makes no charge against the depositor for this work, its idea being to furnish service and thereby to build up and maintain good-will rather than to make a direct profit.

### **Non-Stock Exchange Loans**

With the exception of stock exchange and other loans made over the window, the loan department obtains the material for its work from the credit department of the bank in the regular way for offerings. The loan comes in the form of

a note accompanied by collateral and an offering ticket, each of which items has been duly approved by the officers in charge of granting loans. The negotiating of stock exchange loans is not done by the officers' committees and the credit department, however, and this phase of the work deserves special consideration.

Stock exchange call money is loaned on the board by money brokers who represent banks and other institutions, as well as individuals having money to lend on call. These brokers may work for the lender on salary or on commission, but there is no recognized standard rate to be charged for placing loans. Practically every one of the larger financial institutions places all its stock exchange loans through a broker who divides his time between making loans for it and dealing in securities. Stock exchange time loans are negotiated by a different group of loan brokers who call from bank to bank with their offerings.

### **How the Rate for Call Loans Is Determined**

The rate at which money is loaned on the stock exchange is determined by supply and demand. As the brokers, or the "loan crowd," on the exchange meet together they are able to determine from the offerings and biddings what the market rate is for money. First is announced the renewal rate for a day. This rate is set by a committee of the stock exchange and applies to all loans which are to be continued from the preceding day. During the remainder of the day attention is devoted to new loans. The bid and offered rates which brokers are receiving for loans at the moment are termed the "market rates." These rates, of course, may move up or down during the day according to the supply and demand.

In most instances the bank instructs its broker to loan at the market rate. When the market rate is high, however, it is the policy of the bank the practices of which are described

here, to give preference in the matter of rate to those borrowers who maintain accounts with it. In loaning funds for out-of-town banks and in loaning to other than depositors, however, the bank follows the market rate.

The lending bank determines the sizes of the individual loans which it wishes to have placed. Call loans are made in blocks running from \$25,000 to \$500,000, but \$100,000 is commonly thought of as a minimum. There is an irregular demand for loans in the smaller blocks and it is often impossible to place them at all. In publishing quotations of rates for loans the newspapers and financial bulletins consider only those pertaining to blocks of \$100,000 or more.

After the money broker has received notice of the amount, rate, and blocks in which the bank wishes its loans to be made, he places the individual loans as he finds bidders who are willing to take them under the term he is empowered to make. As he places the loans he notifies the bank of the names of the borrowers, the amounts loaned, and the rates. Later in the day messengers representing each borrower present the collateral for the approval of the bank and receive cashier's checks for the amounts of the loans. The collateral for each loan is enclosed in an envelope which shows on its face the rate, a list of the collateral enclosed, and its market value. The care of the loan department is to see that the collateral is acceptable and that the transaction conforms to the terms communicated to the loan broker. Official approval is given by an officer who signs the cashier's check. For the purpose of record the officer makes indication of his approval by placing his initials on the envelope containing the collateral.

### The Loan Contract

In making stock exchange call loans no note is used. Instead of a note each broker signs and lodges with the bank a contract (Form 57) which covers all the loans which he



**Whereas**, the undersigned expect, from time to time, to borrow money from THE NATIONAL CITY BANK OF NEW YORK (hereinafter called the Bank) and to pledge with the Bank property of various kinds as collateral security for the payment of such loan or loans to be hereafter made by the Bank, Now, therefore,

**It is Agreed** by the undersigned with the Bank, that all property thus pledged with it may be held by it as collateral security for the payment of such loan or loans as well as for the payment of any other obligation or liability, direct or contingent, of the undersigned, or any of them, to the Bank, due or to become due, whether now existing or hereafter arising, and the undersigned agree to deliver to the Bank additional securities or to make payments on account to its satisfaction should the market value of the said securities, as a whole, suffer any decline. The undersigned hereby give to the Bank a lien for the amount of all such obligations and liabilities upon all the property or securities now or at any time hereafter given unto or left in the possession of the Bank by the undersigned, whether for the express purpose of being used by the Bank as collateral security, or for any other or different purpose, and also upon any balance of the deposit account of the undersigned, or any of them, with the Bank.

On the non performance of this promise, or upon the non-payment of any of the obligations or liabilities above mentioned, or upon the failure of the undersigned forthwith with or without notice to furnish satisfactory securities, or to make payments on account, in case of decline as aforesaid, or in case of insolvency, bankruptcy, or failure in business of the undersigned, or any of them, then and in any such case, all obligations and liabilities direct or contingent of the undersigned and each of them, shall forthwith become due and payable to the Bank, and the undersigned shall pay the same to the Bank, and shall deliver to the Bank, without demand, advertisement or notice of any kind, all of which are hereby expressly waived, for any of the said purposes, at any broker's board, or at public or private sale, or in suit to or for the Bank, by mouth or in writing, or by any other means, the whole or any part of the property sold, free from any right of redemption which is hereby waived and released. In case of any sale or other disposition of any of the property aforesaid, after deducting all costs, or expenses of every kind for collection, sale or delivery, the Bank may apply the residue of the proceeds of the sale or sale to make, to pay, or more or all of the said obligations or liabilities to it, whether then due or not due, making proper rebate for interest on obligations or liabilities not then due, and returning the overplus, if any, to the undersigned, who agree to be and remain liable, jointly and severally to the Bank for any deficiency arising upon such sale or sales. The undersigned do hereby authorize and empower the Bank, at its option at any time to appropriate and apply to the payment and extinguishment of any of the obligations or liabilities, heretofore referred to whether now existing or hereafter contracted and whether then due or not due, any and all moneys now or hereafter in the hands of the Bank, on deposit or otherwise to the credit of or belonging to the undersigned or any of them.

The Bank may assign or transfer this instrument and may deliver the said collateral security or any part thereof to the transferee or transferees who shall thereupon become vested with all the powers and rights above given to the Bank in respect thereto and the Bank shall thereafter be forever relieved and fully discharged from any liability or responsibility in the matter. No delay on the part of the holder hereof, in exercising any rights hereunder shall operate as a waiver of such rights.

New York, \_\_\_\_\_

Jan. 5, 1921

John Brown & Son  
By John Brown

Form 57 (a) Loan Contract (face) (Size 8 1/2 x 5 1/2)

makes so long as he continues as a borrower. The contract is a lengthy form of document, but in essence it gives the bank authority to use the borrower's collateral to settle any indebtedness which may be owing from him. Not only does it give the bank authority to sell the collateral which has been lodged with it specifically for the purpose of securing a given loan, but it gives the bank a lien upon all securities and upon the deposit balance of the borrower in case his collateral is not sufficient to meet his loans. The contract also gives the

In consideration of one dollar paid to the undersigned and of the making of the loans referred to in the within agreement, at the request of the undersigned, the undersigned hereby jointly and severally guarantee to THE NATIONAL CITY BANK OF NEW YORK, its successors and assigns, the punctual payment, at maturity, of the loans so made, and hereby assent to all the terms and conditions of the said agreement, and consent that the securities for any such loan may be exchanged or surrendered from time to time, or the time of payment of the said loans or any of them extended, without notice to or further assent from the undersigned, who will remain bound upon this guaranty, notwithstanding such changes, surrender or extension.

Form 57 (b) Loan Contract (reverse)

bank the right to require additional security of the borrower and to foreclose the loan without notice in case the additional security is not promptly forthcoming. The borrower waives notice of the proposed foreclosure in all cases and he agrees to permit the bank to become a purchaser of his collateral in the event of foreclosure if such collateral is sold on the stock exchange, at public auction, or at private sale. Finally, the borrower's contract is a continuing obligation and it mentions no specific loans and no specific collateral. Its effect therefore

is to give the bank a lien upon any property which it may hold for the borrower to meet any obligation which he may owe

### Method of Negotiating Day Loan

The day loan is negotiated directly between the borrower and the bank. As has already been mentioned, many brokers who have occasion at times to use more funds than they have to the credit of their accounts, arrange to supply the needed funds by means of the day loan in connection with which a quantity of collateral is kept on deposit. This collateral is covered by an agreement which is similar in scope to the contract for the call loan but which takes the form of a letter of transmittal accompanying the securities as they are sent to the bank. No note is used in negotiating a loan of this sort. The prospective borrower simply communicates his needs for funds to the loan department which gives him authority to have checks certified up to the amount needed. At the end of the day the balance is restored and the loan closed out.

### Loan Envelope

As the loan comes to the loan department the individual items consist of a note, except in the cases of the call and the day loan, and an approved offering ticket, or in the case of a call loan a report of the bank's money broker and the borrower's collateral. Collateral is always filed in a standard form of envelope, illustrated in Form 58. Brokers prepare their envelopes but the loan department attends to this work for other borrowers. On the outside of the loan envelope is placed the date, the name of the borrower, the amount of loan, a list of the securities enclosed together with the quantities and the market price of each, and the total market price if the collateral consists of stocks and bonds, or value of the security if other than stocks and bonds.

When it is submitted to the bank the material making up

the loan is checked over to make sure all is in order. The collateral and the notes, if any, are checked with the offering

# LOAN

John Brown & Son  
27 Broad Street  
New York  
\$100,000

March 23

6%.

100	Northern Pacific	82	8	200
600	Southern Pacific	101	60	600
200	Consolidated Gas	91	18	200
400	American Int. Corp.	102	40	800
			127	800

Form 58 Loan Envelope (Size 5 x 11)

ticket or with the money broker's report, as the case may be, in order to determine that the amount and rate of the loans are correct. Then the collateral is counted and checked

with the list on the envelope. Before accepting the loan it is necessary that the collateral be examined to see that it conforms to the requirements which the bank sets up for its protection. This examination varies according to the type of security offered.

### Examination of Collateral

In connection with merchandise loans, warehouse receipts and bills of lading are examined with a view to determining that they are bona fide, duly executed instruments, as evidence that the merchandise is in the hands of the warehouse or transportation company. This work has been materially aided by the operation of the Uniform Warehouse Receipts Act and the Uniform Bills of Lading Act which have been adopted by several states acting under the recommendation of the American Warehousemen's Association and the American Bankers' Association, also by the Pomerene Bill of Lading Act passed by Congress in 1916. These acts have contributed much toward establishing uniformity in bills of lading and warehouse receipts, and thereby eliminating the uncertainties in estimating the value of such instruments and reducing the risks of loaning upon this type of collateral.

The condition of the merchandise covered by collateral instruments is determined by means of certificates of weight, of appraisal, or grades, etc., which have been prepared by the various officials of produce, cotton, grain, and other commodity exchanges, or by state officials. In some instances it is necessary that the bank have an appraisal of the commodities covered by the bills of lading or warehouse receipts made by a disinterested party.

The risk of the warehouse itself is also taken into consideration in estimating the worth of warehouse receipts as collateral. It is common to provide protection against this risk by having these instruments accompanied by insurance

policies or certificates covering loss or destruction of the property

The reliability of the warehouseman is also an important element. Only warehouse receipts issued by independent warehousemen are acceptable to the bank. Each commodity exchange association approves of certain warehouses in its vicinity by designating that receipts issued by these warehouses shall be suitable instruments to be passed from buyer to seller and that delivery of these receipts shall constitute good delivery of the merchandise represented in connection with trading on that exchange. The fact that a warehouse has been approved by an exchange is considered favorable, but such approval is not essential to acceptance of the instrument by the bank. The bank relies, rather, on its own knowledge of the credit rating of the warehouseman.

In examining bills of lading the bank is not obliged to be on its guard against loss or damage to the property, since the transportation company is legally the insurer of the goods which it carries. Certain other risks, however, attend loaning upon bills of lading. The bill of lading does not guarantee the quality of the goods which it covers, and in many instances it may be stamped "Shipper's Load and Count" or "Packages Said to Contain" a certain quantity. The value of the bill of lading as collateral for the loan therefore depends entirely upon the credit standing of the borrower.

### Examination of Stock Exchange Collateral

In examining and approving collateral supporting stock exchange loans, the first fact ascertained is that the security is listed on the exchange. The fact that a security is listed on the exchange gives the bank a triple degree of protection: (1) listing is a condition precedent to salability on the exchange in the event that the bank finds it necessary to foreclose, (2) in favorably passing upon an application to list, the committee

of the exchange necessarily passes upon the validity of an issue, and (3) concerns whose securities are listed on the New York Stock Exchange are required to submit periodical reports or statements of financial condition for publication by the exchange. For these reasons listed securities are always required for collateral in stock exchange loans and they are desirable for all classes of loans.

### Good Delivery

In examining collateral, care is taken to see that it is in negotiable form so that it may be sold in case of default by the borrower. Securities are transferred from one owner to another by assignment on the books of the issuing concern. The borrower gives the bank an assignment in blank or a power of attorney empowering it to transfer ownership to the securities in case it becomes necessary to do so. In approving the assignability of collateral the bank is guided by the stock exchange rules for good delivery. The term "good delivery" signifies that the stocks and bonds under consideration are in proper form and that the seller's title to them is such that it may be transferred. These rules cover the kinds of stocks and bonds which can be sold and the units in which they shall be traded, together with the method of executing assignments and powers of substitution. They also designate the qualifications in a legal sense which a person, firm, or corporation must have in order that they may sign assignments or powers of substitution.

### Proportions of Rails and Industrials

After having determined that the collateral is in negotiable form the next care is to see that the kinds of collateral are in the right proportion. Most stock exchange loans are made upon security consisting of part railroad stocks and bonds and part industrial stocks and bonds. The former class is termed

"rails," while the latter is termed "industrials." Each bank has its own opinion as to the relative merits of the two classes as collateral and in keeping with this opinion each has its own policy regarding the amount of the relative proportions of these two classes which it will accept. Due to the greater stability of the railroad securities and to the fact that they have been better known, and hence more readily marketable without loss in the past, many banks favor these securities over the industrials. The bank whose practices this book delineates, for example, makes it a policy to loan upon all-industrials collateral only in rare instances and then at a higher rate, but it lends quite freely upon all-rails collateral.

The bank makes the majority of its loans, however, on mixed collateral. Its policy is to require that at least 50 per cent of the collateral shall consist of railroad securities. Mixed collateral is particularly desirable because quite frequently the market factors which influence the one have little effect on the other, hence the bank distributes its risk by having its loans based upon both. The collateral is accordingly examined for the proper proportion of rails, and in case the proportion is not deemed sufficient the loan is either refused or the broker is told to bring additional rails.

The total number of issues making up the collateral is an important consideration in approving collateral. The risk of the bank is distributed by having several issues represented rather than a very few, while, on the other hand, the fact that too many issues are represented might indicate blocks too small to constitute "good delivery" on the stock exchange or it might indicate that the offering is composed of too many low-priced issues. The total number of shares or bonds contained in the collateral is another important consideration. Too many low-priced issues tend to weaken the collateral. There is no fixed rule, however. Decision is made after consideration of the individual shares offered.



## Margin

After having decided upon the acceptability of the collateral as to character, the next problem is to determine its adequacy. Adequacy of collateral is measured in terms of margin. Margin may be defined as an excess of market price or value of collateral over the face of the loan. It is expressed in percentage of excess of market value over face value. The custom of Wall Street banks is to require a 20 per cent margin on call loans, but certain brokers regularly follow the practice of keeping an even higher percentage than the banks require. This figure of 20 per cent is seldom deviated from by any bank in New York City in making call loans, regardless of the keenness of the competition. In making loans secured by United States Government bonds, however, the margin may be as low as 10 per cent.

## Examination of Non-Stock Exchange Collateral

Unlisted stocks and bonds are examined in much the same way as are those which are listed. The requirements as to margin, proportions, etc., are, however, not standardized and each transaction is therefore subjected to individual consideration. Many issues offered as collateral for a loan are not traded in on any exchange, hence no published quotations are to be had. Prices of such issues are obtained if necessary from some bond house in the vicinity. So extensive is the business of these houses that for each security which is traded in anywhere, there can usually be found some New York house which deals more or less extensively in that security and which is in a position to furnish a reliable quotation. Bank stocks are quite frequently offered as collateral. Many of them, however, practically never change hands. In arriving at the value of such stocks the bank takes the book value, which is readily accessible in its credit files.

### Settlement with Borrower

After the borrower's loan has been accepted by the bank, payment is made to him either by check or by a credit to his deposit account, according to his instructions. Stock brokers are given an engraved identification certificate which they must present to the bank when they pay off the loan and obtain their collateral. This certificate is designed to protect the bank in making deliveries of collateral to the various messengers who call to pay off loans and is worded as follows: "Upon presentation of this order, together with check for the requisite amount, you will please deliver the proper documents to bearer." Each of these certificates contains a code number and this code number is likewise stamped upon the loan envelope.

### Loan Cards

After the loan has been accepted the details are entered upon a loan card (Form 59), of which there is one for each individual loan. The function of the loan card is to contain a record of the transaction from the time it enters the bank until it is closed out. These cards are kept by the margin clerks for their use in recording substitutions of collateral in a readily accessible form, watching margins, and selecting loans to be called in case of need.

There is accordingly a distinctive color for each class of loans, and distinctive shapes to assist in distinguishing merchandise loans from loans made upon stocks and bonds. The loan card contains the name of the borrower, the date, the amount of loan, rate, kind of loan, and a detailed list of the collateral, giving quantities, kinds, market value, and total market value, as in the case of the face of the loan envelopes. In entering loans on the cards the margin clerks also verify the work of the window men in checking prices, extensions, totals, margins, proportions, etc.



each week may be readily compiled for the consideration of the directors of the bank

Postings to the loan ledger are made from the loan cards. At this time the following information is entered: name of borrower, amount of loan, rate of interest, and a list of the collateral. At later dates changes in collateral and in interest rates, interest collected, part payments on the loan, and settlement in full, are entered as the occasion may require. At any time, therefore, the loan ledger shows the condition of each loan being carried by the bank and its history.

Time loans are entered in a tickler according to maturity dates. This book is more like the tickler of the note teller than the tickler of the domestic discount department in that its function is merely to remind the department that certain loans are falling due upon a given date, rather than to serve as a book for journal entries.

### Loans-Made Journal

The loan cards, loan ledger, and tickler contain only memorandum entries. Changes in the accounts of the bank occasioned by making loans are entered in the loans-made journal. In this book the loans made each day are recorded consecutively. The entry covering the transaction of making a loan consists of two parts: the debit represents the increase in the assets of the bank, and the credit represents the settlement made with the customer. Corresponding to these two parts there are two sides to the loans-made journal. The debit side shows the names of borrowers, the rate at which loans were made, and the amounts of the loans as debited to the proper accounts—Demand Loans, Demand Street Loans, Demand Merchandise Loans, Time Loans, Time Merchandise Loans, and Day Loans accounts. The credit side of the loans-made journal shows the credits arising from the method which was used in advancing the funds to the borrower. The amount

of the loan appears on this side as a credit to Renewals, Cashier's Check account, or customers ledgers, according to whether the loan was made in renewal of one already outstanding or whether funds were given to the borrower in the form of a cashier's check or credited to his account

In the case of advances made to borrowers upon warehouse receipts or bills of lading it is quite common for the loan department to handle the transaction as a discount deducting interest in advance. In an instance of this sort, of course, a credit arises to the "Discount Collected But Not Earned" account for the amount of discount, and this book accordingly has a column for recording such credits

The foregoing operations complete what is termed "putting on the loan." In the interval of time between the initial act of making the loan and the final act of receiving payment from the borrower the loan department is occupied with certain activities which are quite distinctive of its work. Among these are caring for collateral substitutions, watching margins, computing and collecting interest, and collecting income from collateral for borrowers. Before considering the work to be done in connection with the payment of loans it is well to consider these interim operations briefly

### Collateral Substitutions and Withdrawals

A peculiarity of the collateral loan is that the borrower is permitted to withdraw portions of the collateral which he has lodged with the bank, substituting other securities in their stead. Much of the usefulness of the secured loan as an instrument of finance arises from this arrangement. By changing collateral, a borrower can finance his operations on the strength of his inventory and still use any portion which he may need.

In keeping with this, stock exchange brokers sell the securities which they have pledged with their banks and withdraw

them for delivery under the sale. When the stock market rises, brokers withdraw the excess of their collateral over the bank's requirements as to margins and they may make part payments upon their loans at various times, each of which transactions necessitates the surrender of a part of the collateral. In withdrawing collateral each broker signs a substitution certificate requesting the bank to deliver certain designated securities to him, and unless he reduces the amount of the loan by payment or the market value of the collateral has increased he requests the bank to accept certain other securities in exchange.

### Trust Receipts

Changes in the collateral of merchandise loans may occur quite as frequently as in the case with stock exchange loans. Borrowers often substitute one commodity for another, or one grade for another of the same commodity. In most merchandise loans the bank permits borrowers to make partial payments and this necessitates the release of a portion of the security. Warehouse receipts are indivisible except by surrendering the document and securing new ones covering the parts into which it is desired to divide the security. When it is desired to release a part of the security covered by a document of this sort the bank requires the borrower to furnish a trust receipt (Form 60) or a certified check covering the full amount of the collateral. It then delivers the collateral to the holder and he withdraws the portion agreed upon, obtaining from the warehouse a receipt covering the amount still in storage. This warehouse receipt is returned to the bank, which then cancels the borrower's trust receipt or returns the amount of his check.

Goods held in storage are quite frequently released for purposes of manufacture, sale, or transportation to another warehouse, etc., or for any combination of these operations.

The borrower obtains the goods from the bank by executing a trust receipt under which he agrees that title to the goods shall remain in the bank, that he will use the commodity released only for the purpose agreed upon, and that he will restore the value of the commodity to the bank after it has served the purpose agreed upon. The trust receipt depends for its value upon the credit standing of the one who executes

New York, <u>April 15</u> 1921	
Received, from THE NATIONAL CITY BANK OF NEW YORK, the following property, held by the Bank as collateral security	
<u>100 bags coffee covered by Bills of Lading</u>	
<u>Car No. 1466 New York Central R.R.</u>	
and in consideration thereof <u>we</u> HEREBY AGREE TO HOLD SAID PROPERTY IN TRUST for the following purposes, viz. <u>transfer to warehouse</u>	
and <u>we</u> will return the said property, <u>as soon as the merchandise can be stored in the warehouse &amp; proper receipt issued</u>	
with due diligence to the Bank, the intention of this arrangement being to protect and preserve unimpaired the lien of THE NATIONAL CITY BANK OF NEW YORK on said property	
<u>Johnson &amp; Parown</u> <u>By - J. P. Johnson</u> <u>Treasurer</u>	

Form 60 Trust Receipt (Size 7 $\frac{3}{4}$  x 5 $\frac{1}{2}$ )

it, but it also lays a moral restraint upon the borrower in that it makes him liable for criminal prosecution for misapplication of the commodity held, or of the proceeds of the commodity in case it is to be sold.

In accepting new collateral in place of released items this new collateral is given the same careful scrutiny as is collateral just being submitted in support of a loan. In considering stock exchange collateral, for example, the collateral must be negotiable and the proposed change must not disturb the

margin of the loan, the requirements as to the number of shares, number of issues involved, and the complexion of the loan—that is, the proportion of rails to industrials making up the total security—must be fully complied with. The signature on the application is also carefully verified so that the clerks may assure themselves that the released collateral is being delivered to authorized persons. The letter of application is filed as evidence of the transaction in case differences arise.

In practice it is not always possible to take time to examine in detail the complexion of each loan as substitutions are made. Accordingly the loan cards are examined at intervals, say weekly, and those borrowers whose loans have undergone changes in quality are notified that they must submit new collateral in order to bring the loan up to standard.

Entry of collateral substitutions is made on the loan cards and in the ledger. On the loan cards each delivery is erased or crossed out and the collateral substituted is entered at the bottom of the list in the usual way. The total market price of the security is then revised in order that it may be evident that the margin is being maintained. In the ledger the date of delivery is stamped opposite each issue which has been released and entries are made of the substituted collateral received. By this means the loan ledger furnishes information as to when a given item of collateral was delivered should inquiry be made.

### **Maintenance of Margins**

It will be recalled that the agreement with borrowers is that the bank may call for additional security to support their loans at any time it sees fit. Where the collateral consists of merchandise and other forms than stocks and bonds it is rarely necessary for the bank to give detailed attention to the matter of margins. Stock exchange collateral, however,



is subject at times to violent fluctuations in value. The loan department therefore maintains a tickler service carrying the quotations from the New York Stock Exchange, and as the market falls to a point where a borrower's margin is not satisfactory, call for additional security is made. In theory the bank may call for additional margin at any time and if such margin is not forthcoming it may sell the collateral and close out the loan. This is very rarely done. In practice, under normal market conditions margin calls are sent out each evening and the broker is required to restore his margin during the next day. Brokers keep their own records of the state of their margins and generally restore the margins promptly, so that it is rarely necessary to call a loan on account of insufficient margin.

When the stock market is inactive the loan cards are examined each week, and thus affords sufficient protection to the bank in the way of margins. In case of a violent downward market, however, a large part of the working force of the department is shifted to the task of watching margins. Under these circumstances it becomes necessary to send out calls for additional security each morning and in some cases to notify borrowers by telephone.

### Changes in Interest Rates

The understanding in connection with the stock exchange loan is that the bank is to charge each day a rate of interest in conformity with the renewal rate quoted on the New York Stock Exchange. In practice, however, the bank does not exactly follow this rate. In the first place special agreements may be made with certain borrowers to the effect that the bank will not raise the rates upon their loans beyond a certain point. As has already been noted, it is also the policy of the bank not to raise its rate above a certain point on loans to those who are its depositors regardless of what the stock

exchange renewal rate may be. On demand loans other than those made on call the rate may also fluctuate, but it usually follows the more stable general interest rate as charged on commercial paper and discounts. In connection with these loans only the larger changes in rate are followed by the bank.

The loan department, after taking such matters of policy and agreement as these into consideration, attends each day to making whatever other changes are necessary. Changes of rates are entered in the loan ledger in order that interest computations may be made when the proper time for collecting interest arrives. A notice of the action of the bank in changing the rate on a loan is mailed to the borrower as soon as possible during the day on which the change takes place. This notice takes the form of a simple card,  $6 \times 3\frac{1}{2}$ , bearing the words, "We mark the rate of interest on your loans—" In addition to serving the function of enabling the borrower to keep his records in order, this notice reaches him in time for settlement of the loan to be made the same day if the new rate is not satisfactory.

### Collection of Interest

By custom of the Street, banks are entitled to collect interest on their outstanding call loans at the end of each month. The interest charge on other demand loans is collected on the same plan. On time loans the bank collects interest every three months. Borrowers also pay interest at the time of settlement of a loan, regardless of what other obligations they may have with the loan department. In collecting a loan the bank mails a statement to the borrower who settles either by sending remittance or by authorizing the bank to charge his account for the amount involved. Bills for interest are entered in the interest book the function of which is to record outstanding bills for uncollected interest. When the bill is paid the account in this book is closed out and entry is made

in the loans-paid journal, to be presently described, crediting the Interest account for the amount received

### Collection of Coupons

During the life of the loan the bank performs certain incidental functions, such as collecting coupons from bonds held as collateral, making comparison of collateral lists, interest rates, and other matters with the records of borrowers, etc. The loan department collects the income from securities only upon the request of the owner. Coupons are sent to the coupon collection department where they are collected and accounted for to the owner in the regular way.

### Collection of Loans

It will be recalled that the agreement in connection with the call loan is that it may be paid by the borrower at his option and it is to be paid at the bank's call. On the part of the bank, call loans are considered a form of secondary reserve. In times of need for funds, therefore, the bank relies in part upon its outstanding stock exchange demand loans to supply the deficiency. In keeping with its policy of furnishing to its customers every accommodation consistent with good business, the bank protects those borrowers who are on its list of customers by calling the loans of others first. The proceeds of such loans are generally sufficient to care for the needs of the bank. So far as the bank is concerned, call loans made to customers are therefore generally permitted to continue for a considerable time.

### Method of Calling a Loan

While by agreement a stock exchange call loan is payable at any time during banking hours, it is a custom of the Street to consider each one as running for at least one day, that is, loans made today are by custom not callable until the following

day, except those made on Saturdays. In calling a loan the bank sends a standard form of notice (Form 61) to the borrower before 12 15 in order to give him time to arrange to pay the loan the same day and thereby obtain possession of the collateral. The broker then has until 2 15 P M to pay his obligation and take possession of his collateral. In paying the loan, whether at his own option or upon call by the bank, the borrower presents a certified check together with the identification certificate which the bank gave him at the time of making the loan. The bank then delivers the collateral.

THE NATIONAL CITY BANK OF NEW YORK

65 WALL STREET

NEW YORK, *April 28 1921*

*John Brown & Son*

KINDLY REPAY US TO-DAY YOUR DEMAND LOAN OF

\$ *100,000* DATED *March 23*

THE NATIONAL CITY BANK OF NEW YORK

Form 61 Notice of Call of Loan (Size  $7\frac{3}{4} \times 3\frac{1}{2}$ )

Since the borrower generally sends a messenger to pay his loan, the bank is obliged to assure itself that the messenger is authorized to receive the collateral to be returned. This is accomplished by means of the identification certificate and by verifying the signature on the certified check. After payment has been made the identification certificate which has been surrendered by the borrower is filed as evidence that payment has been made and that collateral has been delivered.

### Collection of Time Loans

Time loans are collected as they fall due. The tickler indicates those maturing each day. To forward a loan for

collection, as is done in the case of a discount, would result in the release of the security, hence the bank notifies the borrower of maturities and it expects him to send funds in payment. In order to give the borrower ample time to arrange to meet his obligation, maturity notices are mailed some two weeks before the loan is to be paid. The borrower pays by sending a remittance covering the face of the loan and accrued interest, or by having the bank charge his account; then the bank releases his collateral and disposes of it according to his instructions. When the loan is paid, entry is made in the ledger to close out the account and the corresponding loan card is filed away for reference.

### **Prepayment, Part Payment, and Renewal of Loans**

Loans are quite frequently renewed, paid in part, or prepaid. Occasionally borrowers may receive funds which make it unnecessary for them to have borrowed money, and they naturally apply to the bank for permission to prepay their loans. The loaning bank does not encourage this practice, for it may easily be abused by arranging loans when money rates are high and prepaying them when they are low, and if the interest were refunded at the higher rate the borrower might borrow elsewhere at a lower rate to prepay his outstanding obligation. It is usual to compute the interest refund at a rate of interest that can be obtained in case the funds are reinvested. When a loan is renewed the maturing obligation is canceled and stricken from the records as a paid loan would be; then the renewal loan is put on as a new loan.

### **The Loans-Paid Journal**

The various changes in the accounts of the bank occasioned by the payment of loans and interest are recorded in the loans-paid journal. The debit side of this book records the changes in accounts occasioned by the method of payment used by

the borrower. It therefore contains the following information: rate, name of borrower, debit to account involved in the method of payment, as under Renewal Loan, Charge account, or cash, loan number, ledger folio, and debit to Interest account for rebates made on interest in connection with prepayment. The credit side of this book shows the credit to the Interest account for interest collected, and to the asset account reduced, according as the loan paid was a demand, demand street, demand merchandise, time, time merchandise, or a day loan, together with a credit to the Exchange account for exchange assessed on obligations payable out of town in accordance with the clearing house rules.

### Earnings from Loans

The earnings on loans differ from those on discounts in that the latter are paid for in advance while the former are in many cases paid for after they accrue. To find the amount of interest which has accrued on loans during the fiscal month, interest sheets are used. In order to classify earnings according to kinds of loans there is one sheet for each class—demand street, demand merchandise, time merchandise, etc. These sheets are ruled with columns for each rate at which loans run. Each line of the sheet contains the business of a given day. From the loans-made and loans-paid journals the total amount of loans running at each rate is obtained and entry of those amounts is made in the proper spaces on the interest sheets. At the end of the month the total amount running at each rate is found by footing the columns of these sheets. By computing interest at the given rates for one day on the corresponding total amounts running, the total earnings from loans are obtained. This earnings figure is credited to Interest and charged to an asset account entitled "Interest Earned But Not Collected."

During the month payments of interest bills are constantly

being made For such payments the Interest Earned But Not Collected account is credited This account, which appears on the general books of the bank, therefore, shows the amount due the bank for uncollected interest accrued on loans

### Accounting for Loans Made for Customers

A word should be said at this point concerning the loans which the bank makes for its customers These loans are treated with the same care and in the same manner as loans made by the bank for its own account, except the funds are furnished by the customer

As between the bank and the owner of the funds the relation is one of agency The lending or agent bank therefore keeps its principal, the owner of the funds, fully informed as to the details of the transaction At the time of making the loans the bank sends the client a notice giving the rate and a list of the collateral. It also notifies him of all the changes in rate and in collateral See form of notice shown in Form 62

The bank gives the same care in regard to passing on collateral, watching margins, caring for collateral substitutions, changing interest rates, etc., on loans made for customers as it does to its own loans In addition such loans are subject to control by the client He may have the loan called at his option or he may refuse to accept the collateral offered or the interest rate obtained, as he sees fit In addition to exercising its own judgment regarding loans made for customers, the bank also sees that any orders he may send are promptly executed.

Separate records are kept for customers' loans. These consist of a customers' loans made and paid journal, which combines the functions of the loans-made and the loans-paid journals, and a customers' loans ledger, which is the counterpart of the loans ledger

The customer provides the funds to be loaned by sending a remittance or by having his deposit account charged To offset this debit a credit is made to an account termed "Funds Loaned for Customers " As customers' loans are paid off, the

TO First National Bank, - - - - -

Indianapolis, Indiana.

**THE NATIONAL CITY BANK OF NEW YORK**

**LOAN DEPARTMENT**

**MEMORANDUM OF CHANGE OF COLLATERAL**

WE HAVE RETURNED to John Doe & Co., - - - - -

from their loan of - - - - - July 6, 1921

100	U. S. Steel	9
25	U. S. Steel, pfd.	2 7

**RECEIVED**

140	Beth Steel	12
-----	------------	----

New York, 8/3/21



PROOF SHEET		
LOAN DEPARTMENT		
By <i>H. H. White</i> Dist Head <i>CR</i>		
DEBIT	ACCOUNT	CREDIT
<i>505,000</i>	Demand Loans	<i>326,000</i>
<i>1,200,000</i>	Demand Street	<i>310,000</i>
<i>163,125.90</i>	Demand Merchandise	<i>243,678.38</i>
<i>27,000</i>	Time	<i>26,340.87</i>
	Time Merchandise	<i>45,791.56</i>
<i>4,200,000</i>	Day Loans	<i>4,200,000</i>
<i>755,000</i>	Customer's Loans	<i>595,000</i>
<i>595,000</i>	Funds Loaned for Customers	<i>755,000</i>
<i>37.50</i>	Interest Earned Not Collected	<i>1,714.11</i>
	Interest Account	
	Discount Collected Not Earned	<i>927</i>
	Discount Account	
	Cashier's Checks	<i>2,455,036.65</i>
	Prepaid Expense War Revenue Stamp	<i>5.20</i>
	Exchange a/c	
	Sundry	
<i>117,000</i>	<i>Discounted Loans</i>	<i>50,000</i>
	TOTAL	

## LOANS

345

LOAN DEPARTMENT		Date	Mar 15 1921
DEBIT	ACCOUNT	CREDIT	
7,362,163.40	GRAND TOTAL	4,609,562.77	
	DOMESTIC INDIVIDUAL LOANERS		
	Alabama Idaho	49,250	
	Illness Louisiana		
	Main Missouri		
	Montana Ohio		
	Oklahoma F. Michigan		
	Rhode Island Wyoming		
	New York A	350,000	
	New York B		
	New York C	12,900	
	New York D F	2,913,400	
	New York G I	10,232.57	
	New York J L	550,000	
	New York M N	400,000	
	New York O R		
	New York S	132,000.73	
	New York T Z	4,013,375.90	
	TOTAL		
	NATIONAL BANKS		
	Ala. Ida		
	Ill. Kan		
	Ky. Miss	2,49,350.08	
	Mo. N. Y.	201,066.65	
	N. L. Okla		
	Okla. Tex	46,893	
	Tex. Wyo	4,47,311.73	
	TOTAL		
	STATE BANKS, TRUSTS and SAVINGS		
	Ala. Ill	79,930	
	Ind. Miss	50,266.67	
	Mo. N. Y.	50,266.67	
	N. C. S. D.	50,019.44	
	Tenn. Wyo	170,442.70	
	TOTAL		
6,443,567.78	NOTE TELLER		
14,095,731.18	TOTAL	14,095,731.18	

Daily Proof (Size 13 x 12)

proceeds are restored to them by crediting their deposit accounts or sending them remittances. To offset credits made in this way, debits are made to the Funds Loaned for Customers account. The balance of this account therefore shows the liability of the bank to its customers for loans which it holds for them.

In making loans for customers the bank keeps the asset account representing the loan itself separated from those representing its own loans. When made, these loans are charged to an account entitled "Customers' Loans." Likewise when the loan is paid off, this account is credited. The balance therefore represents the amount of loans running for customers.

### Loan Department Proof

At the close of the day a proof of the operations (Form 63) is prepared and sent to the general bookkeepers. Like the proof of the domestic discount department this proof shows a summary of the entries arising from the work of the department. These entries may be summarized as follows:

- 1 The loan accounts—Demand, Demand Street, Demand Merchandise, Time, Time Merchandise, Day, and Customers Loans—are debited for loans made and credited for loans paid.

- 2 The Funds Loaned for Customers accounts are credited for liability incurred to customers for loans made for them and debited when such loans are paid and settlement rendered to the customer.

- 3 Interest Earned But Not Collected account is debited for monthly earnings accrued and credited for payments received for interest.

- 4 The Interest account is credited for monthly earnings.

- 5 The Cashier's Check account is credited for checks issued.

- 6 The customers' accounts are

## (a) Debited for

- (1) Loans which borrowing customers have paid off by having proceeds charged to account.
- (2) Funds to be loaned which customers provide by authorizing the bank to charge their accounts
- (3) Interest which borrowing customers have paid by authorizing the bank to charge their accounts.

## (b) Credited for

- (1) Proceeds of loans made credited to the accounts of borrowing customers.
- (2) Settlement of the proceeds of paid loans made for customers who desire the bank to settle by crediting their accounts

7 Note Teller—debited for the cash items received during the day by the loan department.

## CHAPTER XIII

### BONDS

#### Bank Transactions in Bonds

A bank may engage in security transactions either for its own account or for its customers. Securities held for the bank's account consist of bonds and, if the bank is a member of the federal reserve system, of stock in the federal reserve bank of its district, and possibly stock in other banking corporations authorized by the Federal Reserve Act. The purpose of holding such securities may be (1) to obtain income from them as investments; (2) to obtain certain privileges; and (3) to assist the government in its financing. In handling securities for customers the object may be either to obtain the profits of underwriting or to furnish service, or both.

It is not generally considered good policy for a commercial bank to invest heavily in bonds. While bonds may at times have attractive features their non-liquidity, in the sense that they are not self-liquidating on a short-time basis, stamps them as outlets for investment funds such as those gathered together by savings banks and institutions acting in some fiduciary capacity, rather than for the funds of a commercial bank, which are repayable on demand. It is, however, generally considered safe for a commercial bank to invest in bonds up to an amount equal to its combined capital and surplus since these funds represent the interest of the owners in the business and they are not repayable on demand.

#### Privileges Carried by Bonds

Aside from a certain attractiveness purely as investments, certain bonds carry with them legal rights and privileges which

are, or at least have been in the past, more or less valuable to a bank. Among these privileges should be mentioned those connected with the deposit of bonds to secure the circulation of national banks and to secure public deposits. At the inception of the National Banking Act Congress provided that any bank organized under this act should have the privilege of issuing bank notes to an amount equal to not more than its capital stock, provided it purchased and kept on deposit with the United States Treasurer collateral security in the form of certain United States bond issues to an amount equal to the face value of the proposed bank note issue. The national government also requires that banks which hold public funds and postal savings on deposit shall pledge certain acceptable issues of bonds with the Treasurer to secure such deposits. Most state and municipal governments likewise require the pledging of certain securities by banks which deal with them as depositories and in other relations. Each of these acts was designed to a certain extent with a view to providing the various governments concerned with a ready market for their securities and in the past such acts have offered inducements to banks to become extensive owners of the favored issues.

### Ownership of Stocks

In this same connection should be mentioned the bank's holdings of stock in the federal reserve bank of its district and stock in other banks permitted by the Federal Reserve Act. At its inception the Federal Reserve Act provided that a national bank should come into the new system within a certain time or lose its charter. At the same time the act provided that each member bank must subscribe to and own a portion of the capital stock of the federal reserve bank of its district equal to 6 per cent of the capital and surplus of the member bank. National banks if they desire to do so are permitted

by the Federal Reserve Act to own stock of certain other banks authorized by the act. In the first place a member bank may invest an amount not exceeding 10 per cent of its paid-in capital and surplus in the stock of other banks chartered under national or state law and engaged principally in foreign banking. Several of the large member banks have taken advantage of this privilege with the result that a considerable number of subsidiary banks are operating in the international field. In the second place a national bank may also invest in the capital stock of corporations organized under the so-called Edge Act, but its total investment in the stock of these corporations, together with that in other international banks, cannot exceed 10 per cent of its paid-in capital and surplus.

### **Assisting Government Financing**

Purchasing bonds with a view to assisting the government in its financing hardly needs a detailed description. In times of great public danger, as during the World War, the banks of the United States freely subscribe to the war loans of the government. While in making these subscriptions the banks are actuated in part by a desire to realize income from these securities and in part by a desire to furnish service to those of its customers who wish to purchase these bonds, the whole volume of these operations cannot be attributed solely to these motives. The paramount aim of the bank, after all, in such times is to aid the national government.

### **Purchase and Sale of Securities**

In addition to dealing in bonds as an investment, a bank located in the chief security market of the country is in a position to perform a particularly important service for its customers in making purchases and sales of securities. The individual customer goes to his bank for advice and recom-

mentations as to investments. The out-of-town correspondent in turn often looks to its New York City bank to furnish a similar service. In the actual purchase of securities for investors the banks are likely to be called upon to execute their customers' orders. Again, out-of-town national banks look to their city correspondents to purchase the bonds which they use in securing circulation, public deposits, and for similar purposes, and to sell them when no longer needed. Savings banks and similar institutions look to the same source for bonds in which to invest their funds. Thus the large metropolitan bank becomes an important factor in investing the funds of the whole country—the funds of private investors, as well as those of banks. In such a case the bank usually transacts this business as a service for its customers, making a charge only for the brokerage or other expenses which it may incur.

### Organization for Handling Bonds

From the description of the relation of bonds to banks in general it is readily apparent that the scope of the activities of a metropolitan bank with respect to bonds is most far reaching. In fact, such a bank not only purchases and holds bonds as an investment but it deals in bonds at retail and at wholesale. As a dealer at wholesale, under the meaning of the term used here, the bank participates in underwriting syndicates for placing new issues of stocks and bonds in the hands of investors. In this connection the bank performs the characteristic function of an investment banker. By "dealing at retail" is meant the purchase and sale of stocks and bonds, principally the latter, in the market, either for profit or as an accommodation for customers.

These two last mentioned will be recognized as more properly the functions of a bond house, and it is not considered the best policy for a bank to conduct these operations in



close connection with its regular commercial transactions. In the operation of the bank the practices of which make up the material for this study, therefore, an affiliated or subsidiary bond house has been put in operation for the purpose of engaging in underwriting syndicates and dealing in bonds and preferred stocks at retail. Under an arrangement of this sort the bond department of the bank proper confines itself to purchasing, selling, and holding the bonds and stocks owned by the bank itself, and to executing certain orders for customers. While the work of the affiliated bond house is so closely related to that of the bank that these institutions may be considered as one in so far as their commercial efforts make up a complete financial service to their customers, it is advisable to confine the present discussion to the work of the bank itself. Hence the work of underwriting syndicates will not be discussed here at any length.

### Sources of Bond Supply

The purchase of securities may be made through different sources depending upon their nature. Original issues of government securities, of which the certificate of indebtedness is the one in most common use at the time of writing, are obtained through the federal reserve bank. The bank is notified of the floating of a new issue of these securities some time in advance of its appearance, and the amount of the issue which it desires to purchase for its own account is determined by the management in accordance with the policy which is being pursued in the purchase of these government obligations. In obtaining other bonds the bank purchases them through a broker on the New York Stock Exchange, over the counter, or from an underwriting syndicate. Among these methods of dealing in bonds in New York City, the second predominates—about three-fourths of the volume of trading is done over the counter.

## Purchase Ticket

When the bank official in charge of this division of the work has purchased a block of bonds or subscribed to a government issue, he sends a notice of the fact to the bond department. Here a record of the transaction is at once made upon a purchase ticket (Form 64). These tickets, which are numbered serially, give the date, the name of the party from whom the purchase is made, the par value of the issue, the kind of bonds, whether registered or coupon, the kind of security;

BOND DEPARTMENT		No. <u>858</u>	Date <u>March 17, 1921</u>
To be Bought of <u>Federal Reserve Bank</u>			
Par <u>\$15,000</u>	coupon	Security <u>U.S. Certificate of Indebtedness</u>	
Price <u>100</u>	and Int	Date <u>4-30</u>	Maturity <u>Mat. 15/22</u> Int. Periods <u>From Mar 15, 1921</u>
DELIVERED <u>Series No 7 M 1921</u>			
Cash <input checked="" type="checkbox"/>	Credit Acct. <u>Lawful Reserve</u>	Date <u>Mar 24-1921</u>	Par _____
Regular Delivery	Send Check	No Instructions	
Await Bonds	Confirmed	Principal <u>\$ 15,000</u>	
For Balance see Ticket No. _____	Interest <u>\$ 3.87</u>		
For Original see Ticket No. _____	Total <u>\$ 15,003.87</u>		
Remarks <u>Numbers Taken</u>			

Form 64 Bond Purchase Tickets (Size 7½ x 4)

the price, the coupon rate, the maturity date, and the interest periods. Spaces are also provided for notations as to payment on the bonds, such as cash, send check, credit account, etc. A check mark is placed after the proper notation in this regard and also after the notations "Regular Delivery," "Await Bonds," "No Instructions," and "Confirmed," according to the details which have been received in regard to the purchase. The ticket is then filed away to await the time when the corresponding securities come into the possession of the bank.

### Receipt of Bonds into Vaults

At a time in keeping with the stock exchange rules for making delivery or, in the case of new securities, upon the date of issue, the seller delivers the bonds, which are counted and examined to see that they conform to the bank's order in every way, that all unmatured coupons are attached, that signatures are genuine, etc. In case all is found to be in order the seller is paid by a cashier's check, drawn to cover the amount or a credit passed to his account, if the transaction is to be handled in this manner.

The bonds are then filed in the vaults, the securities of each issue being kept separate from all others. Henceforth whenever an addition or subtraction is made to the amount of an issue held in the vaults by means of a sale or purchase, the issues involved are carefully counted to make sure that the records are correct. The amount of bonds on hand in the vault is indicated by a vault record showing additions, withdrawals, and balances held.

After the bonds have been received the purchase ticket is completed by entering in the space provided for the delivery data, the date of delivery, the par value, the principal, the interest, and finally the total amount paid for the bonds. This ticket now gives a complete synopsis of the transaction, and from it the proper entries are made to the books.

### Bought Register

The most important of the records concerned with the purchase of the securities is the "bought" register, illustrated in Form 65. This register is kept by days, that is, there is a separate section for the work of each day. On the debit side of this book is recorded the purchase ticket number, the rate, the par value, a debit to Interest Earned But Not Collected account for the amount of interest paid the seller, and a debit to the asset account affected for the cost of the prin-

capital of the bonds. There are two of these asset accounts corresponding to the classes into which the bank divides its holdings. United States bonds, which term includes all issues of the United States government, and bonds, securities, etc., which term includes all issues other than those of the United States government. On the credit side is recorded the credit involved in making settlement with the seller—Cashier's Check account or the account of a depositor. In addition to giving a day book record of the purchases made this book also constitutes a journal. At the close of each day the totals of the debit columns "Interest Earned But Not Collected," "United States Bonds," "Bonds, Securities, etc.," and of the credit columns, "Cashier's Checks" and "Depositors' Accounts," are transferred to the daily proof sheet whence they are posted to the general bookkeepers' accounts.

### **Income from Bonds**

Interest earned on bonds is paid by the debtor at regular intervals, usually semiannually. As has already been indicated, the bank keeps its profit and loss accounts on a monthly basis, hence it is necessary to account for the interest accrued each month. Records to care for these accruals appear in the bond ledger to be described later. In this book all bonds of each issue held by the bank are entered in a separate account, e g., all bonds of the United States Liberty First 3½'s issue held by the bank would be shown in the bond ledger account maintained with this issue. As new securities are bought or as sales are made the new balances resulting are brought forward.

The accruals on each issue are cared for as follows. During the current month in a column of the ledger headed "Debit Interest Earned But Not Collected" are entered debits to the Interest Earned But Not Collected account for interest paid to sellers on bonds of the issue purchased. In a column

headed "Credit Interest Earned But Not Collected" are entered credits to this account for interest collected from purchases, as the bank sold bonds of this issue. On the last day of the month, interest accrued on the issue is computed. In making this computation the par value held on the last day of the month is used as the base, the time is the time elapsed since the last coupon or interest payment date for the bonds, and the rate is the coupon rate. The figure obtained in this way is added to the total of the credit column showing interest collected, then the accrual figure from the preceding month plus the interest paid on purchases is deducted. The resulting figure represents the accrual on the particular issue for the current month.

These figures for all issues held by the bank are credited to the Interest account and debited to Interest Earned But Not Collected on the bond department proof, whence the entries are passed to the general books. The accrual figure for each issue is entered in the debit "Interest Earned But Not Collected" column for that particular issue in the bond ledger. When, at the interest period for the issue, interest is collected, credit for the amount is made to the Interest Earned But Not Collected account. By this system the Bond Interest account for each month carries to the Profit and Loss account of the bank the actual earnings on hand. The Interest Earned But Not Collected account is, of course, an asset account which at the close of each month shows accurately the amount due the bank on unpaid interest on bonds.

### Collection of Bond Interest

A close watch on all interest periods is kept. Maturity dates are shown by the bond ledger. Several weeks before the interest falls due coupons from coupon bonds are clipped and forwarded to the coupon collection department. The coupon collection department effects collection and credits the

Interest Earned But Not Collected account of the bond department. Thus as the interest is collected upon any given block of securities the account of Interest Earned But Not Collected is wiped out and there remains but the Interest account as a record of the earnings of the department.

In the matter of collecting interest on registered bonds the book entries are the same but the procedure in collecting is somewhat different. When the bank receives bonds of this class it has the seller execute an assignment in favor of itself or its nominee, the head of the bond department. The bonds are then transferred on the books of the issuing concern. At interest periods the issuing concern forwards a check to the bank. Checks received for this purpose are credited to the Interest Earned But Not Collected account through the bond department direct.

### Pledging of Bonds

As has been previously observed, an appreciable amount of the bonds held by the bank is from time to time pledged to secure various state and United States government deposits, to secure the bank's circulation, to secure trust funds, etc. The bank also pledges bonds as security to foreign banks who accept for its account.

Various methods are employed in holding pledged bonds. In many cases they are lodged with the federal reserve bank. They may, however, be held in the bank itself, in which case they are pledged to a nominee named by the federal reserve bank. In case the bonds are pledged to secure acceptances of foreign banks the securities are turned over to the customers' securities department, which holds them as nominee. In whatever manner the pledged securities may be held, however, they pass out of the possession of the bond department, even though they are held in the bank they are lodged in a separate section of the vault entirely outside of the jurisdiction of the

department While they remain the property of the bank they are subject to a contingent lien in that they may be appropriated in case the undertaking secured by the pledge is not carried out.

To care for the accounting aspects of pledging, asset accounts designating the nature of the pledges are set up Thus there are such accounts as United States Bonds to Secure United States Deposits, United States Bonds to Secure State and Other Deposits, etc When a block of bonds is pledged, entries are made charging the proper pledged asset account and crediting the asset account from which the pledged securities were taken Thus if United States bonds were pledged to secure circulation, the entry would consist of a charge to United States Bonds to Secure Circulation account, and a credit to United States Bonds account Upon the termination of the banking relation necessitating the pledging of any block of bonds, the bonds are again turned back to the bond department and the entry is reversed

In the matter of interest on pledged securities, the nominee of the institution holding the securities acts as the agent of the bank in collecting the interest when due When collections have been made the interest received is forwarded to the bond department where it is handled in the usual way

### **Borrowing and Lending Bonds**

A practice sometimes met with is that of borrowing and loaning bonds. The effect of the monopoly granted to certain issues of United States government bonds especially to serve as collateral for securing circulation, public deposits, etc, has been to give these bonds abnormally high value on the market—a value so high indeed that there has been no profit in owning them Under these circumstances a bank disposes of much of its own holdings of government securities at the

favorable market rate To provide for its needs it arranges with an owner of bonds of the required issue to loan it the amount needed The borrower holds the bonds under a trust receipt For the accommodation it pays the owner a moderate rate of commission. While holding the bonds the bank collects the interest for the customer and this income together with the rate of commission which the bank pays him constitutes an attractive yield on the bonds. These borrowed securities are pledged for the purposes and in the manner previously described To record its liability to the owner, the bank maintains an account termed "Bonds Borrowed" which is credited when bonds are borrowed and debited when they are returned

Likewise when a bank has a surplus of bonds on hand above its own requirements, it loans them to other banks In loaning bonds the securities are charged to an account termed "Bonds Loaned," and turned over to the borrower on proper trust receipt When the securities are returned to the bank the Bonds Loaned account is credited The practice of borrowing and loaning bonds, however, has been largely discontinued in recent years due to decreased needs on the part of national banks for the high-priced government issues, and it no longer forms an important part of the work of the bond department

### **Sale of Bonds**

It must not be assumed that all issues of securities are purchased by the bank and held by it until maturity The bank may sell at any time to take advantage of an appreciation in the market or to obtain additional funds with which to carry on its operations In this same category are sales of original issues of United States government securities to customers, inasmuch as the bank treats this transaction as a purchase made from the government and a sale made to its client.



Upon receipt of an order from an officer to sell bonds a sales ticket is prepared for the purchaser. This ticket is similar in form and composition to the purchase ticket already mentioned. In case funds are received to pay for the bonds before they are ready for delivery, the department prepares a due bill stating that the customer has paid for a certain amount of a series of securities of a certain issue. This bill is signed by an officer of the bank and forwarded to the customer, who holds it as a receipt pending delivery of the securities. When ready for delivery the bonds are counted out and finally delivered according to the agreement made with the purchaser. In the sale of securities listed on the exchange the rules of good delivery are, of course, strictly adhered to.

#### **"Bonds Sold" Register**

At the time of the sale of any security entry is made from the sales ticket to the sold register. This register performs the same function in regard to sales that the bought register does with reference to purchases and is the same in form as Form 65, though slightly different in its ruling. On the debit side of this book are entered the sales ticket number, the rate, and the par value. Checks and other cash items received are sent to the note teller to be sorted and routed for collection, hence the sold register has a column to record such a charge for the amount received from each sale. If any loss has been sustained from selling the bond for less than its book value the amount of this loss is entered as a debit to the Bond Department Profit and Loss account. On the credit side of the register appear credits to the asset accounts reduced by the sales. Unless, as is rarely the case, the bond is sold on its interest date, the purchaser pays the bank for the amount of interest accrued on the security since the last interest date. This amount is credited to the Interest Earned But Not Col-



lected account just as any other amount representing interest collected would be. Any profit realized from the sale due to the rise of the market value of the securities is here credited to the Bond Department Profit and Loss account. At the close of the day the totals of the journal columns of this book are transferred to the departmental proof whence they are posted to the general accounts of the bank.

### Valuation of Bonds

In the study of the bond department the question of adjusting values of bonds and the profit or loss resulting from their appreciation or depreciation in value while in the possession of the bank has been mentioned. Bonds, like stocks, are subject to considerable fluctuations in price, in accordance with fluctuations in the general level of interest rates and changes in the trend of the earning power and strength of the issuing company.

When a security is purchased by the bank both the par value and the market rate at which it was purchased, or the "book value," as it is termed, are entered on the records. The par value, however, is used only in checking and describing the issues, and figuring interest, it never appears as a figure affecting the assets of the bank. Charges and credits to the bond accounts are made only at the book value of the security. The intention is to have the book value agree approximately with the current market value. The term "approximately" is used because in practice it is not worth while, or even possible, to change the book value of bonds to agree with each change in market price. At intervals the inventory of bonds held is gone over and the book values written up or down to correspond to the current market price. The amount of profit or loss occasioned by this operation is debited or credited to the Bond Department Profits account, as the case may require.

### Records of the Department

In keeping with the negotiable nature of securities, the department maintains, in addition to the bought and sold registers already described, certain auxiliary records covering every detail of the transaction to which the bank is a party. These records also serve as a valuable source of information for answering inquiries received from the bank's customers regarding securities over which some controversy may have arisen. The principal auxiliary records are

1. The bond number book
2. The bond ledger
3. The security cards

*Number Book* The bond number book contains a record of the purchases, sales, and holdings of each issue by bond numbers. It is divided into two sections—the bought, and the sold. When the bonds are received, the date, the number of the purchase ticket upon which the transaction is recorded, the denomination of the bond and the individual number of each bond received, are recorded. As this is done a stamp is placed on the purchase ticket stating that the numbers of the securities described thereon have been recorded in the number book. When the bonds are sold the numbers are entered on the sold side of the number book, denoting that they have passed out of the bank's possession. This book is of great assistance in tracing bonds through the department, in detecting lost, stolen, or counterfeit bonds, etc.

*Bond Ledger* Another record of importance is the bond ledger. In this ledger a complete record of the bonds is maintained from the time of their purchase until their final disposition. For convenience there are two volumes, one for United States bonds held by the bank, and one for all other securities. A separate page is devoted to each issue held by the bank and a complete description of the issue, the rate,

when due, and interest periods, is noted at the top of the page. Each entry in the ledger shows the name of the company or individual from whom the bonds were purchased or to whom they were sold. On the debit side information relating mainly to the purchase of the security appears. This is taken from the bought register and contains the following information: the date, the ticket number, the price, the par value, and the book value. In addition, the debit side of the ledger shows the amount charged to Bond Department Profit, if any, for loss due to selling the bonds at less than book value. To the credit side of the ledger is posted the data regarding sales as taken from the sales register. This contains the par value, the book value, and the bond department profit, if any, occasioned by selling at more than book value. The difference between the book value of debits and credits in the ledger at any given time is the total value of the securities being held by the bank. Should an issue of bonds which the bank holds fall due, be called for payment, or be sold in its entirety, the ledger sheets carrying the record of the issue are taken from the ledger and filed in the department for future reference should any question concerning them arise.

In the ledger important data concerning the interest on the securities is shown. The date at which interest is due is recorded and also the amount due. This ledger space is consequently used as an interest tickler, dates on which interest payments are due on bonds held by the department being taken from it by the clerks in charge of this phase of the work. When the interest is paid the date on which payment was received is entered in the proper space provided for that information. The ledger also contains details of the Interest Earned But Not Collected account, as has been already indicated.

*Security Cards.* For ready reference concerning any

security held, and to check the accuracy of the ledger, a card file is maintained. There is one security card, as these cards are called, for each issue held by the bank. On each card appears the name of the issue, the maturity date, and the interest dates. The card is divided into two parts—one part for purchases, and one part for sales. When securities are purchased entries showing the name of the party from whom the purchase was made, the date, the par value, and the book value, are made in the purchase section of the proper card. When a sale is made, the date, the name of the person to whom sold, the par value, the price at which sold, and the balance held by the bank, are recorded. These security cards are an important departmental record, since they furnish a quick and accurate source of information on matters pertaining to a given security.

### **Supplementary Statements and Reports**

Two statements which greatly facilitate the official work in the supervision of the bond department and the general policy employed in regard to it are the statement of bond maturities and the statement of daily transactions. These supplementary records are prepared for the use of the bank's officials. It is important that the management of the bank know not only the true financial position of the institution as of a given day, but also that they look into the future in so far as it is possible. The maturity of a bond issue of which the bank is a large holder and the prospect of having the resulting idle funds to reinvest is a particularly important consideration for formulating the investment policy of the institution. To furnish information regarding maturities, a statement of bond maturities is prepared. This statement gives a record of the bonds falling due in less than one year, in from one to two years, two to three years, three to five years, five to ten years, and all over ten years. Another

important report is the statement of transactions for the day. This statement, which is sent to the cashier and the executive managers, shows the bonds on hand at the close of the business, their disposition if pledged, and a résumé of every transaction made during the day.

### Bond Department Proof

A proof of the day's operations (Form 66) is prepared and forwarded to the general bookkeepers' department as a basis for the entries which this department makes to the control accounts of the bank. The basis for these entries, as has been previously observed, are the bought and sold registers and the earnings book. A summary of the characteristic entries follows:

1 Bonds, securities, etc.—this asset account, which represents the amount of securities other than United States bonds held by the bank, is debited for all securities purchased and borrowed and for the amount of securities which are returned to the bond department by pledgees. It is credited for all securities sold, pledged, or loaned.

2 U S Bonds on Hand—this account, which is similar to the former but includes only United States securities, is debited and credited exactly as is the Bonds, Securities, etc., account when United States bonds are purchased, borrowed, loaned, sold, or pledged.

3 U S Bonds to Secure U S Deposits, U S Bonds to Secure Bills Payable with the Federal Reserve Bank, U S Bonds to Secure War Savings Stamps and Thrift Stamps, U. S Bonds to Secure Acceptances of Foreign Banks, U S Bonds to Secure State and Other Deposits, and U S Bonds to Secure Circulation; U S Bonds to Secure Trust Department Funds—these accounts are charged when United States bonds are pledged for any of the purposes implied in the titles and credited when the bonds are released and returned to the bank.

4 Other Bonds to Secure Acceptances of Foreign Banks; Other Bonds to Secure U S Deposits, Other Bonds to Secure State and Other Deposits, Other Bonds to Secure Trust Department Funds—these accounts, which are the counterparts of those mentioned in the preceding paragraph except that they cover bonds other than those of the United States government, are debited when bonds other than United States securities are pledged for the purposes implied in the titles of these various accounts, and they are credited when the bonds are released by the pledgees and returned to the department

5 U S Bonds Loaned—this account representing bonds loaned to customers is charged when United States bonds are loaned by the bank and is credited when they are returned.

6 Other Bonds Loaned—this account is debited when bonds other than United States securities are loaned and credited when the bonds are returned

7 Proceeds U. S War Savings Certificates, Stamps, and Thrift Stamps—this account, which represents the bank's liability to the government for sales of these issues made to customers, is credited for the amount of sales of these stamps and certificates when sold to the public and it is debited once each month for the entire amount, at which time a check is issued to the government for the amount due

8 U S Bonds Borrowed, and Other Bonds Borrowed—these accounts are credited when the bonds are received and debited when they are returned to their owners.

9 Interest Earned But Not Collected—this account is charged as interest is earned on the bonds held by the department and when payment is made to sellers for accrued interest; it is credited when interest earned is paid and when purchasers pay the bank accrued interest.

10 Interest—this account is credited for interest earnings on securities each month It is further divided into sections,



BOND DEPT. PROOF			DATE <i>March 17, 1917</i>
DEBIT	ACCOUNT	CREDIT	
<i>18,000</i>	Bonds Securities, etc.		
<i>3,066,000</i>	U. S. Bonds on hand	<i>1,215,000</i>	
<i>450,000</i>	" " to secure U. S. Deposits	<i>1,101,000</i>	
	" " " " R. P. with F. R. B.	<i>1,200,000</i>	
	" " " " W. S. R. and T. S.		
<i>750,000</i>	" " State and other Deposits	<i>750,000</i>	
	" " " " Condition:		
	" " " " Loaned		
	Proceeds U. S. War Sav. Cert. Stamps and Post Stamps		
	Customers Ex. Fund } Postage		
	A/C Securities } Insurance		
	Other Bonds to secure accept. of Foreign Banks		
	" " " " U. S. Deposits		
	" " " " State and other Deposits		
	" " " " Loaned		
	" " " " sold with agreement to repurchase		
	U. S. Bonds Borrowed		
	Other Bonds Borrowed		
	Legal Reserve with Federal Reserve Bank	<i>15,000.00</i>	
	Cashier's Checks	<i>15,000</i>	
<i>225.00</i>	Interest Earned—Not Collected	<i>3.97</i>	
	Interest		
	Interest—Normal Tax Exempt	<i>225.00</i>	
	Interest—Income Exempt	<i>91</i>	
	Bond Prg.—Profits		
<i>4,586,370.00</i>	TOTAL	<i>4,299,230.97</i>	

BOND DEPT PROOF		Date <i>Mar 17 1921</i>
DEBIT	ACCOUNT	CREDIT
<i>A 214 774.47</i>	<i>DEPT OF FINANCE</i>	<i>A 297 734.94</i>
	<i>LOANERS</i>	
	<i>Anthony Webb</i>	
	<i>Elmer Leake</i>	
	<i>Miss Moore</i>	
	<i>Martha Olin</i>	
	<i>William Perry</i>	
	<i>State School Wyoming</i>	
	<i>New York A</i>	
	<i>New York B</i>	
	<i>New York C</i>	
	<i>N = York D-F</i>	
	<i>N = York G-I</i>	
	<i>N = York J-L</i>	
	<i>New York M-N</i>	
	<i>New York O-U</i>	
	<i>N = York S</i>	
	<i>New York T</i>	
	<b>TOTAL</b>	<i>166</i>
	<b>NATIONAL BANKS</b>	
	<i>Atch Sea</i>	
	<i>St Sea</i>	
	<i>St M F</i>	
	<i>M H T</i>	
	<i>M C Olin</i>	
	<i>Ch. Toss</i>	
	<i>Tot. Wks</i>	
	<b>TOTAL</b>	
	<b>STATE BANKS</b>	
	<b>SAVINGS AND SAVING</b>	
	<i>Atch Sea</i>	
	<i>St M F</i>	
	<i>M H T</i>	
	<i>M C Olin</i>	
	<i>Tot. Wks</i>	
	<b>TOTAL</b>	
	<b>FOREIGN BANKS</b>	
	<i>C and M A-C</i>	
	<i>D-F</i>	
	<i>G-H</i>	
	<i>I-M</i>	
	<i>O-L</i>	
	<b>TOTAL</b>	
	<b>FOREIGN T-B</b>	
	<i>Country A-C</i>	
	<i>D-F</i>	
	<i>G-H</i>	
	<i>I-M</i>	
	<i>O-L</i>	
	<i>Foreign Companies</i>	
	<b>TOTAL</b>	
	<i>Due to Depositor</i>	
	<i>Due from State Bank</i>	
	<i>Due from State Bank</i>	
<i>15, 165.17</i>	<b>NOTE TELLER</b>	
<i>A 297 734.94</i>	<b>TOTAL</b>	<i>A 297 734.94</i>

Daily Proof (Size 13 1/2 x 17)

"Interest—Normal Tax Exempt" and "Interest—Income Exempt," to facilitate making the bank's income tax return to the government

11 Bond Department—Profits—this account is charged for all losses sustained by the bank due to selling bonds below the book value, and is credited for all profits made by the bank due to selling above the book value.

PRACTICAL  
BANK OPERATION  
—  
BOOK II



## CHAPTER XIV

### COMMERCIAL CREDITS—IMPORT

#### Nature of Import Commercial Credits

After the loan and discount, the commercial credit is the most important form of extension of bank credit. A commercial credit, or commercial letter of credit, as it is sometimes termed, may be defined as an instrument issued by a bank in behalf of one of its customers authorizing an individual or firm to draw drafts on itself, or on one of its correspondents for its account, under certain conditions stipulated in the credit.

While the use of commercial credits extends to transactions in connection with domestic and foreign business, by far the most important use is to facilitate the importation and exportation of merchandise.

#### Advantages to the Exporter

From the standpoint of the seller of goods, the commercial credit method of financing offers the advantage of providing cash for each shipment upon delivery of documents in his own country. A credit permitting drafts to be drawn on a large, well-known international bank creates prime bankers' bills and these may always be discounted at a most favorable rate. Whether an exporter operates under a time credit or a cash credit he is therefore enabled to offer his goods at lowest prices. Furthermore the seller is relieved of the uncertainties of extending credit to the buyer, this function of extending credit is shifted to the buyer's bank, which is the agent best fitted to pass upon the credit standing of the importer.

### **Advantages to the Importer**

The importer is not obliged to reimburse the issuing bank until maturity of the draft, and by obtaining release of the merchandise against the usual trust receipt, he may manufacture or sell his goods and realize long before the acceptance falls due. The importer has also the reasonable assurance that the shipment will be made in conformity with the conditions as expressed in the letter of credit, and the fact that the bank grants him credit usually indicates that he is regarded as of good standing. He has the full advantage of his credit standing inasmuch as he deals primarily with his bank, which is well acquainted with him.

### **Bank's Profit Under Commercial Credits**

The banking parties to the credit obtain their direct profits from the transaction in the form of moderate commissions. In addition to their commissions those banks which do a large international business participate in discounting, collecting, or making payments under the foreign exchange items which arise from these credits. Again, the banks lend only their credit, since usually they do not part with a dollar in funds until they have been paid by other parties to the credit.

### **Dollar Credits Versus Foreign Currency Credits**

Commercial credits may be classified as dollar credits or foreign currency credits according as they authorize drafts to be drawn in dollars or in foreign currency.

Prior to the outbreak of the war in Europe and the passing of the Federal Reserve Act it is safe to assume that fully nine-tenths or an even larger fraction of the credits issued to cover importations into the United States were passed through London in the form of sterling credits, that is to say, credits available by drafts drawn in pounds sterling on London. Requests for the issuance of credits available by

drafts in United States dollars on New York were extremely rare and were issued only in exceptional cases

One of the important accomplishments of the Federal Reserve Act was to remove the prohibition against accepting drafts under which the national banks had been operating. Under authority granted by the act, member banks may accept drafts which arise out of a transaction involving the importation or exportation of goods, or the domestic shipment of goods, or those secured by readily marketable goods in storage, or drawn for the purpose of furnishing dollar exchange.

The amount of drafts accepted by a bank and the time which the acceptances may run are limited by the act. Any national bank may have outstanding at any one time acceptances aggregating 50 per cent of its capital and surplus. A bank may apply to the Federal Reserve Board and receive permission to have outstanding acceptances up to 100 per cent of its capital and surplus, but in no event may acceptances against domestic transactions exceed 50 per cent of the capital and surplus of the bank. No acceptance may have a maturity later than 6 months after it is accepted. The amount accepted for any one person, firm, or corporation must not exceed 10 per cent of the bank's capital and surplus. This 10 per cent limitation, however, does not apply where the bank is secured by some actual security growing out of the same transaction as the acceptance, the security must remain with the bank during the time the acceptance is outstanding. It should also be mentioned that this 10 per cent limitation is over and above the 10 per cent limitation placed on loans and discounts for any one person.

In addition to the foregoing permissive regulations a member bank may also accept, after receiving authority from the Federal Reserve Board, drafts drawn upon it for furnishing dollar exchange, up to 50 per cent of its capital and surplus. Drafts thus accepted must mature within 3 months.



Since member banks have been accorded the privilege of accepting such drafts, conditions with respect to dollar credits have changed materially and at the time of writing<sup>1</sup> dollar credits predominate

### Advantages of Dollar Credit

The dollar credit is of special importance to every American merchant who is interested either directly or indirectly in the importation of commodities of any character. A study of the advantages accruing from this form of credit will demonstrate the desirability of its general employment as the vehicle for financing not only our own imports, but also those of other countries. Primarily a dollar credit is more economical than those drawn in most foreign currencies, for the initial commission cost of issuance is lower. Secondly it is based on a known quantity, the dollar, a factor of great importance in days of extreme and violent fluctuations in the exchange rates, and therefore all exchange risk is eliminated from the operation so far as the importer is concerned. Maturities drawn under dollar credits are due and payable in dollars on a given date, and no question arises as to what the exchange rate on some foreign point may be 90 days after acceptance of the bill.

### Clean and Documentary Credits

Commercial credits may be classified as documentary and clean credits, depending upon the conditions with which the accredited party, or beneficiary—as the one in whose favor the credit is drawn is called—is required to comply before he can realize under the credit.

Under a documentary credit the beneficiary is required to present certain documents to the negotiating bank before he can obtain payment or acceptance of his draft. Under a clean

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<sup>1</sup> October, 1920

credit no such procedure is necessary; the negotiating bank honors the beneficiary's draft when it is presented with the letter of credit. The documentary credit is generally used to cover shipments title to which can be readily passed by negotiable documents, while the clean credit is used to cover such transactions as transfers of funds made by a home office to its foreign agent or branch and other transactions not readily embodied in negotiable documents.

Documents required under a credit ordinarily consist of a commercial invoice, a consular invoice, and a full set of ocean bills of lading to the order of the New York bank. At times additional documents are required, such as pure food certificates, weight lists, certificates of analysis, disinfection certificates, or certificates of origin.

Credits may also be made available against warehouse receipts and railroad bills of lading, forwarders' receipts, or express companies' receipts, with the understanding that these documents are to be returned either to the beneficiary, a forwarding agent, or some other party named in the credit or to be appointed by the beneficiary for the purpose of making transshipment and exchanging them into the necessary ocean documents as enumerated above.

It develops at times that the beneficiaries under the credits require financial assistance in obtaining the merchandise and preparing it for shipment to the port of embarkation, and in order to meet these contingencies bankers embody in their credits what is known as the "red clause." The bankers making payments under the "red clause" do so as a rule against trust receipts, warehouse receipts, or any other documents used generally in connection with collateral loans, so that the interests of all parties involved are duly protected. It may at times also be necessary to allow the beneficiary to draw clean drafts under a documentary credit. This is always with the understanding that the banks are protected and that

in due course shipping documents will be delivered in full, covering such advances

### **Confirmed and Unconfirmed Credits**

Credits may be established as confirmed and unconfirmed credits. A confirmed credit is one which cannot be canceled or modified without the consent of all engaging parties, whereas an unconfirmed credit is subject to revocation at any time by the issuing bank.

### **Fixed and Unlimited Credit**

The capacity or face amount of the credit may be one of two kinds: the fixed, that is, non-revolving, and the revolving credit. The non-revolving credit is issued for a fixed amount up to which drawings may be made by the beneficiary. As each draft is drawn and honored, the amount of the credit is permanently exhausted by the face amount of the draft. When the amount for which the credit was opened is exhausted the credit ceases to exist and if the total drawings made by the beneficiary amount to less than the face amount of the credit, the unused balance expires automatically by limitation. The revolving credit, on the other hand, represents a continuing obligation of the issuing bank within a definite term to meet drafts up to a fixed maximum at any one time.

There are several forms of revolving credits. The most common form permits the beneficiary to draw drafts up to the face amount of the credit, each draft temporarily exhausts the credit by the extent of its (the draft's) face value, and the amount thus drawn becomes again available at maturity or upon payment. A second form enables the beneficiary to draw a certain amount in one draft. When that bill has matured and has been paid another similar sum may be drawn in a similar way, and so on in this manner until the term of the credit has expired. Still another form may

allow the beneficiary to draw up to a certain amount in any one month or any one week or by any one steamer until the credit expires by limitation. Credits under which the beneficiary may avail himself up to a certain amount within a certain period, say for instance, monthly, may be cumulative or non-cumulative. If cumulative, undrawn portions of the amount authorized for previous periods are available for drawing in later periods, if non-cumulative, they are not.

### Import Commercial Credit Department

To take care of the great amount of detail work entailed by the import operations, the import commercial credit department is divided functionally into three sections, the credit-issuing, the documentary, and the ticket sections. The credit-issuing section prepares the transaction for submission to the officers for their approval, it makes the arrangement with the applicant and the foreign correspondent, and it keeps the records pertaining to this phase of the work. The documentary section receives documents from abroad as shipments are made under the credits, examines them closely to make sure that they are drawn in conformity with the credit, and releases them to the importers. The ticket section attends to collecting from the importer, settling with the foreign bank, and making the necessary bookkeeping entries.

### Passing Upon Credit Rating

A request for the opening of a commercial letter of credit is quite similar to an application for a loan or a discount and it is treated in much the same manner. Under a commercial letter of credit the bank guarantees to honor drafts if drawn in accordance with the terms of the credit and it looks to the importer for reimbursement, hence the credit standing of the applicant, or the importer, is the paramount consideration in passing upon an application for a commercial credit. The

desirability of the applicant as a credit risk is therefore surveyed from all angles. The bank also establishes the fact that the importation covers readily marketable merchandise. Specifically, examination of these points is carried out as shown in the paragraphs just following

### Method of Application

The bank requests the American importer first of all to make his application for a commercial credit upon its own special form (Form 67). This application form brings out the salient points of the transaction and it contains such information as is necessary to enable the officers of the bank to approve the credit. The importer may submit his application either direct or through his local bank; in fact, banks throughout the country freely avail themselves of the services of their New York connections in financing the foreign business which comes to them. Instead of issuing their own commercial letters of credit they turn applications from their customers over to their New York correspondents guaranteeing the same. Under a ruling of the Comptroller of the Currency, however, a national bank is forbidden to guarantee the engagements of its clients; hence, a bank of this class makes its applications in its own name on a form furnished by the issuing bank and the importer executes a separate guarantee.

### The Offering Slip

As the first step in the process of opening the credit an offering slip is prepared (Form 68) upon which is noted the total liability of the applicant under outstanding import credits. This liability appears under three headings. (1) the value of previous shipments held by the applicant under trust receipt, (2) the contingent liability, i e., unused balances of pre-existing credits, and (3) the amount of documents which are being held for various reasons. In the case of a credit issued

upon the application and attendant guarantee of a bank the issuing bank looks primarily to the guarantor. The offering

# APPLICATION FOR IMPORT COMMERCIAL LETTER OF CREDIT

New York, MARCH 25, 1921.

THE NATIONAL CITY BANK OF NEW YORK,  
NEW YORK.

Dear Sirs.—

We beg to request you to establish a Documentary Letter of Credit under our Guaranty, on the following terms and conditions.—

Amount, \$50,000. \_\_\_\_\_

Favor of JOHN SMITH & COMPANY, SHANGHAI, CHINA, \_\_\_\_\_

Account of BROWN & COMPANY, NEW YORK, \_\_\_\_\_

Available by drafts @ FOUR MONTHS SIGHT, \_\_\_\_\_

Covering Invoice value of RAW SILK, \_\_\_\_\_

Plain Machine Commodity

Shipment to NEW YORK \_\_\_\_\_ and to be effected within \_\_\_\_\_

Duration of the Credit to be limited to JULY 1, 1921. \_\_\_\_\_

Documents required. INVOICE, CONSULAR INVOICE, BILLS OF LADING TO ORDER OF THE NATIONAL CITY BANK OF NEW YORK. \_\_\_\_\_

Insurance to be effected by BROWN & COMPANY UNDER OPEN POLICY WITH ATLANTIC MUTUAL INSURANCE CO. \_\_\_\_\_

Credit to be opened by mail—~~advice~~ \_\_\_\_\_

Shipping documents for Custom House entry, to be sent to BROWN & COMPANY \_\_\_\_\_

Remaining documents to be sent to \_\_\_\_\_

Very truly yours,

*Brown & Co*  
*By J R Smith, Treas*

Form 67 Application for Commercial Credit (Size 8½ x 11)

ship accordingly indicates the liability of the guarantor rather than that of the applicant. The offering slip is sent to each

of the other departments of the bank which extend credit accommodations to customers. In these departments the following data are noted: (1) amount of liability under acceptances made by the export commercial credit department, (2) foreign bills purchased, (3) discounts, and (4) loans. After this information is completed the offering ticket is submitted for

FOREIGN DEPARTMENT	
Date <u>March 25-1921</u>	
Offering by <u>Brown &amp; Co.</u>	
Address <u>New York City</u>	Business <u>Importers &amp; Exporters</u>
Guaranteed by _____	
Amount <u>\$50,000</u>	<u>at 4 mo. sight pay sight on New York</u>
<u>Documents to be delivered against trust receipt</u>	
Delivered \$ <u>234,000</u>	C. C. export acceptances \$ <u>10,235</u>
Contingent \$ <u>842,000</u>	Exchange purchased \$ _____
Holding \$ _____	Discount Department \$ <u>325,000</u>
Total \$ <u>1,076,000</u>	Loan Department \$ _____
Approved { <u>JMY</u> <u>MBS</u> <u>mm</u>	Credit dept.

Form 68 Commercial Credit Offering Slip (Size 8 x 7)

approval both to the officers in charge of the applicant's territory and to those officers who have charge of the territory of the beneficiary. The approved ticket is then returned to the department as an authorization to proceed with the opening of the credit, afterwards the approved offering ticket is read at the officers' meeting and passed to the auditors, and finally it is filed away in the folder of the applicant in the credit

department     Another copy is placed in the file of the guarantor

### Arrangement with the Customer

The second step in issuing the credit consists of drawing up the agreement, or obligation, as the contract between the bank and its customer is termed. Distinctive agreement forms (Form 69) are provided for foreign currency and dollar credits, and of these two there are different forms for credits opened at the request of national banks and those opened for others. The face of the agreement is a copy of the letter of credit itself and the reverse side enumerates the terms under which the credit is to be used. The following are some of the more important provisions in which the applicant concurs. He agrees to furnish the bank with funds at any time he is requested to do so, but at least one day before the maturity of dollar drafts drawn under the credit, and if he wishes to pay at the check rate he agrees to refund at least 12 days before the maturity of foreign currency drafts, or one day, if he wishes to pay at the cable rate, or he agrees to remit an approved demand draft in time for it to reach the foreign correspondent on or before the date of maturity, he is bound to give the bank a lien on the goods covered by the credit and to absolve the bank from any loss arising from causes beyond its control, and, if requested to do so, he must pay or give security before the bank surrenders the documents representing merchandise imported under the letter of credit. This agreement is sent to the applicant or guarantor for signature and returned to the bank.

### The Letter of Credit

Full details of the credit are then communicated by the issuing bank to all parties concerned. This may be done by sending a formal letter of credit (Form 70) to all engaging



DOLLAR CREDIT**The National City Bank of New York****Copy of Letter of Credit No. 19500**

New York, MARCH 25, 1921.

\$50,000 - U.S. CURRENCY

JOHN SMITH &amp; COMPANY.

SHANGHAI, CHINA

Gentlemen

*We hereby authorize you to value on*

THE NATIONAL CITY BANK OF NEW YORK, NEW YORK,

for account of BROWN &amp; COMPANY, NEW YORK,

up to an aggregate amount of FIFTY THOUSAND DOLLARS, UNITED STATES CURRENCY

available by your drafts at FOUR (4) MONTHS SIGHT,

when accompanied by Bills of Lading for MERCHANDISE

INVOICE TO READ: RAW SILK, SHIPMENT TO NEW YORK

*Bills of Lading for such shipment must be made out to the order of The National City Bank of New York and, together with invoices, must accompany the drafts**A Duplicate of such invoice, with Consular Certificate attached together with one copy of Bill of Lading, must be sent by the Bank or Banker negotiating draft direct to The National City Bank of New York, New York, by mail, attaching to the draft a statement to that effect**Insurance TO BE EFFECTED HERE.**Any draft drawn under this credit must state that it is "drawn under Letter of Credit N. C. B. No. 19500 - dated New York, MARCH 25, 1921." and must be advised to THE NATIONAL CITY BANK OF NEW YORK, NEW YORK.**We hereby agree with bona fide holders that all drafts issued by virtue of this Credit and in accordance with the above stipulated terms shall meet with due honor upon presentation at the office of THE NATIONAL CITY BANK OF NEW YORK, NEW YORK, if drawn and negotiated ON OR BEFORE JULY 1, 1921.**Very truly yours*

(OVER)

NEW YORK, MARCH 25, 1921.

THE NATIONAL CITY BANK OF NEW YORK  
NEW YORK CITY

DEAR SIR:

In consideration of your issuing your Letter of Credit No. 19500 as per copy attached we hereby agree to its terms and bind ourselves to pay the amount of each acceptance under it to you in cash at least one day prior to the maturity of such acceptance, or at any time you may request it and we hereby give you a specific claim and lien on all goods and the proceeds thereof for which you may come under any engagements under said credit on all policies of insurance on such goods and on all bills of lading given therefor with full power and authority to take possession and dispose of the same at discretion such claim and lien to cover also all charges for expenses and commissions. We hereby authorize you to charge our account with you with any and all amounts that may at any time or times, be owing from us to you hereunder.

Neither you nor your correspondents in SHANGHAI shall be responsible for any loss arising from any difference in quality or character of merchandise imported under this credit from that stipulated and expressed in the invoice accompanying the drafts nor for correctness or genuineness of documents nor for delay or deviation from instructions in regard to shipment nor for any other cause beyond our control.

Your charge for commission under such credit shall be ~~one~~ percent for such part as shall be used.

Merchandise imported under this credit shall be paid for or approved security lodged with you, in your discretion before surrender of the documents. All securities which shall be received by you hereunder may be held and applied by you also to secure all other indebtedness or liability existing or which may hereafter arise from us to you.

All goods imported by us under this or any other credit issued by you or their proceeds whether the draft against the same shall have been paid or not or whether the goods shall have been delivered to us or not may be held by you as general collateral security for any and all indebtedness to you, arising at any time or times from credit extended in us or from any and all letters of credit issued by you under which we may be entitled to import goods.

You are also authorized to surrender to us or our nominees from time to time, any merchandise shipped under this credit or the bills of lading therefor under your usual form of trust receipt signed by us.

This letter of credit can only be revoked with the consent of all parties interested.

*Brown & Co*  
*By J. R. Smith, Treas.*

SIGNATURE OF IMPORTER



# THE NATIONAL CITY BANK OF NEW YORK

Letter of Credit No. 19500

\$50,000 U.S. CURRENCY.

Issued March 25, 1934

JOHN SMITH & CO., INC.,

SHANGHAI, CHINA.

We hereby authorize you to cash on  
THE NATIONAL CITY BANK OF NEW YORK; NEW YORK,

for or credit of BROWN & COMPANY, NEW YORK,  
up to a aggregate amount of FIFTY THOUSAND DOLLARS, UNITED STATES  
CURRENCY,  
as shall be by us drafted at FOUR (4) MONTHS' TIME,  
when accompanied by Bills of Lading for SHAGGYHIE,  
IN 1000 TO BEAD SHAG SILK SHIPPED TO NEW YORK.

Bills of Lading for such shipment must be made out to the order of the National City Bank of New York and together with invoice, warehouse receipts, the drafts, copy of bills of lading must be sent by the Bank or Branch upon delivery draft direct to the National City Bank of New York New York by mail, attaching to the draft a statement to that effect.

Payment TO BE EFFECTED HERE.

Any draft drawn under this credit must state that it is drawn under Letter of Credit 17414, 19500 dated New York, MARCH 25, 1934 and must be addressed to THE NATIONAL CITY BANK OF NEW YORK, NEW YORK.

We hereby agree with bona fide holders that all drafts issued by us hereunder, except and in accordance with the above stipulated terms, shall meet with due honor when presented at the office of THE NATIONAL CITY BANK OF NEW YORK, NEW YORK of date or before date indicated - ON OR BEFORE JULY 1, 1934.

Yours respectfully,

# SPECIMEN

parties or, if there is need for haste, a cable notifying the foreign correspondents of the issue of the credit and at the same time an informal advice is sent to the applicant

The information shown on the letter of credit will, of course, vary with the type of credit. As a rule the details of the sale are not inserted, for such specifications as price, quality, quantity, etc., are more directly a matter of contract between the vendors and the buyers cannot well be controlled by the letter of credit. Rather the letter of credit is designed to cover the financial part of the transaction and the understanding is that neither the domestic nor the foreign bank is held responsible for any losses arising from an unauthorized departure from the terms of the contract. Thus the instrument contains the name of the issuing bank, number assigned to the letter, date and face amount of the credit, name of the accepting or paying bank—if drawn in a foreign currency—name of the beneficiary, name of the importer, tenor of drafts to be drawn, documents required, nature of transaction being financed, whether insurance is to be provided by the shipper or importer, and duration of the credit. At the end there appears the statement of the issuing bank that drafts drawn under the letter will be honored if drawn in accordance with the conditions of the credit and within the specific time limit.

In the case of foreign currency credits the bank issues the credit instrument in triplicate. The original and duplicate are sent to the applicant who sends the original to the shipper. The third copy is mailed to the bank which is to act as accepting or paying agent abroad. The two banking parties generally will have entered into standing agreements concerning the general terms of the arrangements whereby the one is to accept or pay drafts under credits opened by the other. On the other hand the letter of credit instrument, or cable passing from the one to the other for each specific credit, serves as

authority for paying or accepting under a given transaction and transmits the necessary special instructions

In the case of dollar credits, the bank draws up only two copies, inasmuch as it acts as its own paying or accepting agent. Both copies of the letter of credit are sent to the applicant who forwards the original to the beneficiary as he does in connection with foreign currency credits.

### Operation of Import Credit

The method of procedure under a credit can be explained most clearly by outlining the method of financing a shipment under a typical import commercial letter of credit

A bag manufacturer located in Kansas City, Missouri, orders burlap from Calcutta, India. The dealer in India wishes to receive payment either in the currency of his own country or in that of some other country whose currency is readily converted into his own. The English pound sterling is the most desirable in India; hence the exporter asks that the buyer open a confirmed letter of credit in his favor which will provide him the value of the shipment in pounds sterling. The importer sends an application properly signed to New York, say to the National City Bank of New York, and upon the strength of his credit standing (occasionally the bank may require deposit or collateral security) the bank issues a letter of credit authorizing the exporter to draw sterling drafts at 90 days' sight, for example, for the amount of his shipment, on one of its London correspondents, the London Joint City and Midland Bank, Ltd., London, England. The New York bank advises the London bank of its action, and it forwards the original and duplicate of the letter of credit to the importer in Kansas City and a third copy to the London bank. The importer forwards the original of the letter to the exporter abroad.

Upon receipt of advice that the credit has been issued the

exporter makes the shipment in conformity with the terms of the credit and presents to his bankers, usually for discount, his 90 days' sight draft on the London Joint City and Midland Bank, Ltd, London, England, with documents attached, receiving payment therefor at the bank's buying rate for 90 days' sight draft on London. After he has received his money in this way the exporter is out of the transaction except for his contingent liability to the discounting bank as drawer of the draft.

The Calcutta bank will send one set of the documents to the National City Bank direct, and the remaining documents with the draft to its correspondent in London instructing the latter to present the draft to the drawee bank for acceptance, either for the purpose of having it rediscounted and the proceeds credited or with instructions to hold the item until maturity, in which event the face amount of the draft less charges, if any, will be credited to the account of the Calcutta bank.

The London Joint City and Midland Bank, Ltd, will refer to the corresponding letter of credit which it received from New York and, finding the documents in conformity with the terms of the credit, will accept the draft and advise the issuing bank of such acceptance by means of a letter of advice to which there are attached the shipping documents. The New York bank releases the shipping documents to the importer under a trust receipt under the terms of which he agrees to reimburse it before maturity of the draft abroad. At maturity of the draft the London bank charges the account of the New York bank with the face amount of the draft in accordance with previous arrangements.

Since the outbreak of the war the majority of the credits handled by an American bank are dollar credits. Under these instruments the foreign exporter is authorized to draw drafts on the issuing bank. He accordingly draws his draft and

negotiates it with his local bank. The exporter's local bank then sends the draft to its New York correspondent and this correspondent, if other than the issuing bank, presents the item over the window of the import commercial credit department of the issuing bank for acceptance or payment as the case may require.

### Receipt and Examination of Documents

The incoming items mentioned in the two preceding paragraphs furnish the material for the work of the documentary and the ticket sections of the department. The documentary section attends to receiving and examining the documents and releasing them to the importer, while the ticket section attends to collecting funds from the importer, settling with the foreign bank, and making all the necessary book-keeping entries.

As indicated above, the bulk of the documents are received through the mail from abroad. Such items are accompanied by a letter of advice from the foreign bank. A considerable number of the items, however, are taken over the window. In such instances the presenter is given a receipt and requested to call later for the cashier's check or acceptance, in order that the bank may have time to make sure that everything is in order before it acts. The required cashier's check or acceptance is delivered to the customer against surrender of his receipt which is then filed as a record of the transaction.

In the meantime before the bank makes a cash payment or accepts a time dollar draft the documents are thoroughly examined to ascertain if the exporter has complied with the terms of the credit. The bank as the disbursing agent for the customer is required to conform with his instructions as embodied in the letter of credit. The documents are carefully checked against the terms of the credit and should discrepancies be found they are brought to the attention of the

importer, who is requested to send instructions as to how the bank is to proceed in the matter. The customer may instruct the bank to honor in spite of the discrepancies, or he may signify his refusal to accept the shipment unless certain conditions are complied with, in which case the transaction is entered in a turn-down book and the presenter is apprised of such refusal. The documents may either be returned or, as is usually the case, the buyer may make some arrangement with the vendor which is acceptable to the bank and will enable it to continue the transactions.

### Cash Payments Under Dollar Credits

When the bank has determined that all is in order it makes reimbursement to the presenter. This reimbursement may consist of an immediate payment of cash or credit to an account. In such a case tickets are prepared and payment is made according to the wishes of the presenter of the documents.

### Acceptances Under Dollar Credits

Under the majority of dollar credits, however, the bank accepts time drafts. These acceptances are handled in the following manner. A detailed description of the dollar acceptance is entered in a register termed the "acceptance register," which serves the function of recording the acceptances made by the commercial credit import department. This book contains the following information: number of acceptance, date, amount, maturity date, drawer and his address, credit number, for whose account, by whom presented, and nature of the shipment. After a sufficient number of acceptances have accumulated both the acceptances and tickler slips (see page 394) are taken to the proper officer, who signs the acceptances and records his approval of the transaction by placing his initials on the tickler slip. The acceptances are then delivered



to presenters of documents against receipt in the usual way or, if received direct from foreign correspondents by mail, such acceptances are either discounted or held until maturity, according to instructions.

### Release of Documents

In cases where a shipper draws a sight draft and the bank advances him money against the presentation of documents, the customer is required to make immediate payment to the bank and he obtains his documents without impediment. Under acceptance credits, however, the bank does not have to advance funds on arrival, but merely loans its credit by placing its acceptance on the draft. Under a credit of this sort by the usual release of the documents against trust receipt the importer is given the benefit of the time that the draft has to run to enable him to convert the merchandise into cash with which to reimburse the bank at the maturity of the draft. In all import credit transactions the release of documents against trust receipt to the ultimate consignee is approved by two officers in charge of the applicant's territory, and one officer in charge of the territory of the shipper.

In releasing documents to an individual or firm whose application for a letter of credit does not bear the guarantee of a bank, the bank usually delivers these documents under a trust receipt by means of which the importer gives it a prior lien on the shipment as security for his agreement to provide the bank with funds at the proper time. Proper time means one day before maturity if the acceptance is drawn in dollars, and 12 days before maturity if drawn in foreign currency, if the customer wishes to pay at the check rate of exchange, or one day if he wishes to pay at the cable rate.

Under certain conditions, while an importer may ask a bank to issue a credit available by long drafts, the bank may insist that it be reimbursed at the time of the arrival of the

documents or acceptances of the drafts. In this case, the bank would allow interest for the unexpired time of the drafts. This interest rate is based upon the amount to be anticipated, the number of days involved, and the discount rates fixed by the federal reserve bank. It also happens occasionally that long credits are established with the understanding that the merchandise upon arrival is to be stored and insured in the name of the issuing bank and that this merchandise or any portion of it is to be released only upon payment.

In dealing with a customer whose application for a commercial credit bears the guarantee of a bank, however, the bank releases documents on the strength of such a guarantee and it does not require a trust receipt to be executed. It nevertheless sends its regular form of receipt to the guaranteeing bank which it recommends that the latter have its customer execute for its own protection. This form is accompanied by the following notice:

We enclose herewith trust receipt such as we usually exact from our clients, and would suggest that you have your customer sign same and retain it in your files for your own protection.

As far as we are concerned, a mere acknowledgment on your part on receipt of documents will meet our requirements.

### Collection at Maturity

Under commercial credits authorizing time drafts to be drawn, the bank has the absolute obligation of meeting its own acceptances as they fall due, or of reimbursing foreign banks at maturity for acceptances made in its behalf. At the same time it looks to importers to furnish it with funds to meet these obligations. In order to effect these collections promptly, the maturity dates of the bank's own acceptances and of the foreign currency drafts are brought to attention by means of an acceptance tickler file and a foreign currency tickler file.

respectively. These files are composed of a large number of compartments, one for each day of the month, extending over a period of two months. Each compartment is labeled with a day of the month and contains tickler slips representing items which fall due on that day. There are two forms of tickler slips, one for foreign currency items and one for dollar acceptances. The foreign tickler slip specifies the name of the importer together with the amount of the draft in foreign currency and the amount converted into dollars, also the commission of the New York bank as well as that of the foreign bank is indicated, together with the New York and the foreign maturity date. The tickler slip for dollar acceptances omits mention of a foreign bank and carries the acceptance number stamped on the draft.

At the proper time, as ascertained from the tickler, a bill covering the face of the draft plus commissions is sent to the customer in time for him to provide funds in payment. Thus he does by sending a remittance or by having his account charged. The proper amount of dollars for the bill to the customer is obtained in the case of foreign currency credit by converting the foreign bill into dollars, according as the customer desires to use the check or cable rate of exchange prevailing at the time the bill is sent out. In importing goods under a foreign credit, therefore, the importer has to reckon with fluctuations in exchange rates, while in importing under dollar credits he knows the exact dollar amount that he will be called upon to pay to the accepting bank at maturity.

### Anticipation and Increase of Credits

Occasionally an importer desires to anticipate payment of a draft accepted under one of the bank's credits. In such an instance the bank may permit the customer to do so and it would allow him interest for the unexpired time of the draft. On the other hand it may be desired to increase, extend the

duration of, or amend a credit which has been issued. A request for such increase, extension, or amendment, is referred to the officers as an application, as a new credit would be, and if the request is granted the importer is required to furnish an additional guarantee.

### Settlement with Foreign Bank

At maturity the foreign bank pays its acceptance made under the letter of credit. At that time it charges the amount of the payment plus its commission to the account of the American bank. The import commercial credit department of the American bank cares for this settlement by means of tickets crediting its account with the foreign bank for the proper amount. This credit is offset either by a debit to the customer's account or by a remittance received from him.

### Payment of the Bank's Acceptances

Should the transaction involve a dollar credit the outstanding acceptance of the bank is paid in the usual way at maturity. If the draft has been held by a local bank, a member of the New York Clearing House, on a discount or collection basis, that bank presents the item for payment through the clearings. Frequently it may come for payment through the mail or over the window. In any event the department honors the maturing draft and debits "Acceptances under Commercial Credits—Foreign."

### Records of Credit Department

*The Liability Cards and the Credit Cards.* The bulk of information pertaining to import credits is carried on two sets of cards termed the liability cards and the credit cards (Form 71). A liability card is kept for each importer. It shows the total amount and number of credits issued for him as well as payments thereunder. Since the bank in issuing

a letter of credit has obligated itself either to accept drafts or make payments under its own dollar credits, or to furnish cover for payments made by foreign correspondents, the balance unused on each credit constitutes a contingent liability of the bank. These cards therefore show this contingent liability, classified by applicants for letters of credit, and every draw-

OR AVAILABLE WITH <i>National City Bank of New York N.Y.</i>										TERMS OF CREDIT <i>4 Mo sight</i>		AMOUNT <i>\$50,000.00</i>		To Draw on <i>John Smith &amp; Co. Chicago Ill.</i> No. <i>195500</i>
OPENED THROUGH FOR ACCOUNT OF <i>Brown &amp; Co</i> <i>New York</i>														
GUARANTEED BY <i>Brown &amp; Co</i>														
AGAINST <i>Raw silk to New York</i>														
INSURANCE EFFECTED BY <i>Buyers</i>														
DOCUMENTS REQUIRED <i>Invoice, consular invoices</i> <i>Bills of lading</i>										DATE <i>Mar 23/21</i>		EXPIRY <i>July 1/21</i>		
DELIVER SHIPPING DOCUMENTS TO <i>Brown &amp; Co</i>														
OTHER DOCUMENTS TO COLLECT FROM <i>do</i>														
COMMISSION <i>DEBITOR'S END</i>														
SHIPMENT QUANTITY <i>250 Bales</i>		DATE <i>July 1</i>		DOCUMENTS BY <i>1</i>		FORWARDED TO <i>Brown &amp; Co</i>		MEMORANDUM BY <i>J. B. Smith</i>		NO. OF DRAFTS <i>1</i>		DATE <i>Nov 10</i>		
								TO <i>Buyers</i>		DATE <i>Nov 10</i>				

Form 71 Customer's Credit Card (Size  $11\frac{1}{2} \times 9\frac{3}{4}$ )

ing under it. While, however, an importer usually has but one liability card, containing a synopsis of all the letters of credit issued in favor of various foreign exporters, he may have a large number of credit cards, one for each individual credit opened. The liability cards are filed alphabetically by names of importers, the credit cards are stamped with the number of the letter of credit and are filed numerically.

*Credit Issued Book* A credit issued book is kept in which is entered in the credit column the amount of each credit when issued, and in the debit column the value of all acceptances and payments as made. Unused balances of credits are also debited after sufficient time has elapsed for drafts drawn under a particular credit to reach the bank. The credit balance of each credit is the contingent liability of the bank on Commercial Letters of Credit—Import. The primary function of this book is to serve as a summary of the liability cards for the purpose of readily determining the total contingent liability of the bank under letters of credit. For the purpose of this record all foreign currency items are converted into dollars at an arbitrary rate.

*Daily Record of Credits Opened* Certain details essential to the work of preparing statistics in the department are entered in a daily record in which the credits are listed in numerical order. On the first of the month reports are compiled from this book showing: (1) the value of imports by countries and by commodities during the previous month, (2) the total amount and number of commercial credits issued during the past month, and (3) the percentage of dollar credits as compared with foreign currency credits. A list is also compiled showing the daily requirements of foreign exchange for the following month to furnish cover for outstanding commercial credit obligations. The traders receive a copy of this list in order that they may take this factor into consideration in ascertaining their position and make their provisions for cover when needed.

In addition the department prepares: (1) a daily list of all dollar drafts accepted, (2) a daily list of the amounts of documents delivered against trust receipts on the previous day, and (3) a daily list of commercial letters of credit issued. This last-mentioned list is for the use of the directors of the bank at their regular weekly meeting.

*Cross-Index by Beneficiaries and by Guarantors* The credit issuing section also keeps a cross-index by beneficiaries and one by guarantors to facilitate the tracing of shipments

### Summary of the Accounting Work

Entries showing changes in the direct liability of the bank are made by debit and credit tickets rather than by means of a departmental proof. It seems advisable to give a brief summary of these entries as kept in the bank on which this book is based in order to make clear the bookkeeping work of the department

1 The account, *Acceptances of Foreign Banks under Commercial Credits*, representing the actual liability of the bank to provide cover for outstanding acceptances of foreign banks made under the bank's letters of credit, is credited for each acceptance made by a foreign bank according to its advice. This account is debited at maturity of the draft, or before if the draft is anticipated, and at the same time the account of the foreign bank is credited

2 The account, *Acceptances of the National City Bank under Commercial Credits—Foreign*, which shows the bank's actual liability under dollar credits, is credited for acceptances of the bank when made and debited when they are paid

3 *Commercial Credit Issued—Foreign Currency* is merely an interdepartmental account which shows the contingent liability of the bank to meet foreign drafts not yet issued but which the beneficiary can draw under the terms of outstanding letters of credit, and is credited for the face amount of each foreign currency letter of credit issued, the amount of dollars for the credit being obtained by conversion at an arbitrary rate. This account is debited as foreign banks accept drafts, thereby making the liability of the American bank actual rather than contingent. It is also debited for the amounts of canceled or expired credits,

4 Commercial Credit—United States Currency is exactly like the account described in the preceding paragraph except that it applies to dollar credits instead of to foreign currency credits

5 Customers' Liability—Acceptance of Foreign Banks under Commercial Credits account, which represents the liability of customers of the bank to furnish cover for drafts accepted by foreign banks under letters of credit, is debited when foreign banks advise that they have accepted drafts and credited when customers make payments.

6 Customers' Liability—Acceptances of the National City Bank under Commercial Credits—Foreign Import, which represents the liability of customers to furnish cover for the bank's own acceptances as they mature, is debited for drafts which the bank accepts and credited for payments which customers make

7 Commissions account, which represents the bank's profits under commercial credits, is credited for the gross commission charges and debited for adjustments

8 Customers' Expense Fund—Account Cables, showing the amounts of cable charges and other expenses incurred for customers, is credited for the amount of such expense incurred and debited when payment is made.



## CHAPTER XV

### COMMERCIAL CREDITS—EXPORT

#### Export Credit Department

In the opening discussion of the general subject of commercial credits it was stated that the typical commercial credit transaction involves four parties thereto—an importer and his bank, termed the "issuing bank," together with an exporter and his bank, termed the "paying bank." The previous chapter gave a description of the import, or credit-issuing, phase, the export, or paying, phase still remains to be disposed of. Rather than follow through a credit issued by the New York bank and observe how the cycle is completed in the dealings of the foreign bank with its client, it is preferable to study the export phase at close range in the work of the export commercial credit department, which is a complement of the work of the import commercial credit department.

Just as the New York bank is called upon to establish import credits for American buyers desiring to purchase abroad, so banks located in foreign financial centers are requested to open credits for clients who wish to buy in this country. The New York bank through its export commercial credit department acts as paying agent under these foreign credits just as the banks abroad perform that function under credits issued by the New York bank through its import commercial credit department.

There is a greater flow of commodities out of this country than into it and it is therefore to be expected that the volume of work handled by the export department exceeds that of the import department. The unequal balance of trade is also reflected in the types of credits predominating, for the time

being at least, in the work of these two departments. In the American import market the buyer has the upper hand, hence the importer is usually able to get very liberal terms, and import credits largely take the long-time acceptance form. The American export market, however, is a seller's market and owing to the demand for his products abroad the exporter is usually able to obtain cash payments. Accordingly most of the credits handled by the export commercial credit department are straight credits. In total, however, the export commercial credit department, acting as it does in the capacity of paying agent for a large number of foreign banks which operate under widely different conditions, comes into contact with every conceivable form of commercial credit, while the import department comes into contact only with the relatively few forms preferred by its own bank in issuing credits.

Before discussing the work of the export commercial credit department it is well to discuss some types of credits not found in the import phase of the work.

It has been noted that when the bank upon the practice of which this work is written issues its own credits, i.e., the import credits, it issues either a straight or an acceptance credit. Under the former type the beneficiary is authorized to collect a sight draft drawn on the paying bank, while under an acceptance credit he is authorized to draw a time draft and have it accepted. In addition to these two types there are also negotiation, guarantee, and authority-to-purchase credits. Under a negotiation credit the negotiating bank does not become the drawee of the drafts; rather the beneficiary draws upon his purchaser and the negotiating bank is instructed to negotiate, or in other words to discount this draft for him. Negotiation credits may be issued with or without recourse to the beneficiary for dishonored drafts.

There are two types of guarantee credits. Under one type the paying bank on the strength of the guarantee of a foreign

bank simply advises the exporter that his draft up to a certain amount will be honored abroad. It assumes no obligation for payment, the beneficiary must receive his funds from the issuing bank or from the importer. Under the second type the paying bank issues its own guarantee that the beneficiary's draft will be honored abroad. The term "guarantee" as used in this connection must not be confused with the same term as used in connection with the act of guaranteeing that payments will be made under credits entered into by an out-of-town bank on behalf of its clients. Under an authority-to-purchase credit the paying bank advises the beneficiary of the credit that it will purchase his drafts with or without recourse to him at their face value. An authority-to-purchase credit drawn without recourse is often spoken of as a "banker's credit."

### Reimbursement Credit

It has already been noted that the two banks which are concerned as principal parties in the transaction settle with each other by means of charge and credits to their accounts kept with each other. In some cases, however, a bank whose credit standing is unimpeachable may make some bank with which it does not maintain an account a paying agent under one of its credits. A credit opened under such circumstances is termed a "reimbursement credit," from the peculiar way in which the paying bank reimburses itself for its outlay. The paying bank makes the required advance to the accredited party in the funds of his country, then it draws a draft upon the issuing bank for the equivalent amount in foreign currency, which draft it forwards for collection to one of its correspondents located in the vicinity of the issuing bank.

The export, or paying, phase of a commercial credit transaction consists mainly of four operations

1. Receiving of credits opened

2. Informing the beneficiary of the credit.
3. Making advances to the beneficiary as he uses the credit
4. Reimbursing the bank for these outlays

To perform these operations the export commercial credit department is divided into sections each of which cares for the work in connection with credits opened at the request of customers in a certain geographical district. These districts are divided in accordance with the volume of the work. In addition to these sections there is one to care for domestic credits. Each of these sections is in charge of a head clerk and it is composed of (1) a correspondent and a cable clerk who take care of the credit receiving and advising functions, (2) a checker and several payment men who examine the documents and perform the paying functions, and (3) an investigator who has miscellaneous duties. A check-issuing, a bookkeeping, and a filing section are auxiliary to the above-mentioned five divisions.

### Advices of Credits Opened

Arrangements covering the general terms under which commercial credits are to be opened are embodied in standing agreements between the bank and each of its foreign correspondents and branches. However, just as under import credits the New York bank advises its foreign correspondent of the details of a particular credit by sending a letter of credit instrument, so do foreign correspondents send advices to the New York bank giving details of each credit they wish to open. These advices may take the form of a letter of credit similar to that sent abroad by the import commercial credit department, or it may consist of a less formal letter of advice or a cable message. Some foreign branches of the bank send a duplicate copy of the customer's application which serves the purpose of an advice admirably. Details of stand-

ing agreements are kept on file and these files are revised from time to time as new instructions come in

When the department receives an advice by letter it determines that the details conform to the general instructions in effect between the bank and the foreign correspondent or branch. Then the department proceeds to gather the information necessary to authorize the transaction. The signature appearing on the letter needs to be verified inasmuch as the instrument is in effect a draft payable in instalments. This verification is made by the signature control department. For the information of the officer who will pass on the transaction, an investigation is also made to ascertain the size of the balance kept by the foreign bank or firm opening the credit. In the case of a confirmed credit the total contingent liability of the foreign bank or firm under letters of credit which have already been established, is also recorded on the instrument. The letter of credit is then sent to the officer in charge of the applicant's territory for approval.

### **Advising Beneficiary of Credit**

At this time letters of advice and a credit card detailing all the essential features of the credit are prepared. The letter is written in quintuplicate. The original copy is mailed to the customer, as has just been indicated. The second and third copies constitute material for filing the details of the transaction, while the fourth copy is for use of the officers at their daily meeting. The fifth copy of the letter is made upon a large card termed the credit or beneficiary's card (Form 72). This card is similar both in function and appearance to the beneficiary's card used with an import commercial credit. On each card is stamped the number of the credit. As the credit cards are completed they are filed alphabetically by names of beneficiaries. The function of the credit card is to show the details of each letter of credit from the time

it is opened until it is finally used up or canceled. Accordingly in addition to being an exact copy of the credit as it is advised

March 25, 1921	
American Coal Co., Inc., 200 Broadway, New York City	When referring to this credit, please mention our NO 55555
Dear Sirs:  We are pleased to inform you that we have been requested to open a credit in your favor under the terms and conditions stipulated below:  Opened by Copenhagen Laane og Diskontobank, Copenhagen, Denmark, cable 3/24/21 Account F Prausling Broedrene Amount Up to \$20,000 Available by draft at sight on us bearing credit no F E 55555 Covering About 5,250 tons of coal, per sailing vessel "Slaven" from New- port News to Koreser NOTE: All insurances covered abroad  Drafts drawn under this credit must be presented not later than April 11, 1921 unless sooner revoked  Documents required: Full set ocean bills of lading issued to order and blank indorsed Plain invoice in triplicate	
AMOUNT OF CREDIT Cable 4/2/21 - increase to \$50,000	CHANGE A/C OF Above bank  SPECIAL INSTRUCTIONS Cable rec'd 3/28/21 - authorizes us to pay advances to the Captain of the "Slaven" up to the amount of \$5,000. out of the credit amount
EXTENSIONS	CANCELLED BY _____ DATE _____
DISPOSITION OF DOCUMENTS	

Form 72. (a) Beneficiary's Card or Credit Advice (face) (Size 8½ x 10¾)

to the beneficiary, the credit card provides detailed records of each shipment and payment made under the credit, together

with any changes which may be effected in the terms of the credit by the foreign bank. After having advised the beneficiary, the bank also sends a card to its foreign correspondent informing it that the credit has been opened pursuant to its instructions.

When a credit is opened by cable it is handled in much the same manner as a letter credit. A test word takes the place of a signature as a means of authentication, the cable is sent to the bookkeepers for the balance, and to an officer for approval, and the contents of the cable are typed upon the credit card. In the case of a cable credit the beneficiary is

DATE AND AMOUNT OF PAYMENT Basis			DOCUMENTS SENT						
	AMOUNT		B/L	In. Doc.	Trade	Gen. Inv.	Rec'd of Trade	Part of Check	Trade
Apr 5	29 545 00	Covering 3,270 tons Pocahontas coal shipped per sailing vessel "Slavan" from New York to Korea, B/L dated 4/3/21. Charges according to advice to Captain.	1/3		1/3		1		

Form 72 (b) Beneficiary's Card or Credit Advice (reverse)

usually advised of the credit by telegram and a confirmation of this telegram goes forward by mail. It is also customary for foreign banks to confirm by letter their cables opening credits. Record of the cables is therefore kept and compared with the letters when the latter are received. Such confirmation is noted on the beneficiary's card. The letter takes precedence over the cable in authority, hence should it lend an interpretation to the transaction different from that of the cable, the credit card is changed to conform with the letter and the beneficiary is advised of the change. After a credit has been opened, the foreign customer very often alters it by making such changes as extending the time limit, increasing

the amount, or amending the terms. All changes of this nature are noted upon the credit cards and the beneficiaries are advised of them.

### Negotiation of Drafts Drawn under Credits

In the course of time the American exporter prepares his shipment and presents the documents stipulated in the credit to the bank, together with his draft covering the proper amount. These documents come through the mail, over the counter or from a domestic department such as the city collection department or check desk. The bank, of course, cannot honor these drafts until it has made sure that everything is in order. Accordingly payment is not made immediately. A receipt is given to the presenter of the documents requesting him to call later for his payment or accepted draft. A carbon copy of this receipt constitutes a payment slip which is to accompany the document through the process of examination and approval. A third copy of the receipt remains in the bound book which contains the blank receipts and these various third copies constitute a register showing the documents delivered.

The documents are next delivered to the filing section where the corresponding credit card is extracted, the set of documents with the credit card and payment slip attached is then examined by one of the payment clerks assigned to the section handling the work of the territory of the foreign importer.

### Examination of Documents

The point has already been stressed that the chief function of the export commercial credit department is that of acting as paying agent for the foreign bank and indirectly for the foreign importer. In that capacity it is incumbent upon the bank to hold the presenter of the documents rigidly to the terms of the credit before parting with any of its client's



money The work of the department, then, is largely that of examining and re-examining the documents to make sure that they conform in every respect with the instructions of the foreign buyer. The exporter may not be a regular customer of the bank and little may be known about his credit standing. If, then, the bank should accept and pay for documents which diverge in a minor respect from the stipulations in the credit, the foreign buyer might find it advantageous to shield himself behind this technicality, as in the case of a falling market or unfavorable exchange rates, and refuse to take the goods. Inasmuch as the seller is out of the transaction and it may be impossible to recover from him the bank may have to take a considerable loss in disposing of the shipment. Therefore all possible precautions are taken to protect the foreign client and safeguard the bank.

Accordingly the credit card is examined thoroughly by the payment clerk in order that he may become familiar with its terms and ascertain that it has not been exhausted or canceled and that the expiration date has not been passed. The documents are then checked against the instructions appearing on the card as to the specifications of the shipment—the price, quantity, and nature of the merchandise. The insurance certificates are carefully examined to make sure that they amply cover the risk, that they accurately describe the merchandise, and that they are negotiable in form. Brokers' cover notes presented in lieu of insurance certificates are not accepted unless they are approved by the department head, for they do not give the particulars of the insurance which they represent nor do they represent the obligation of an insuring company. The bank also requires that the bills of lading be negotiable in form if the terms of the credit do not specifically call for non-negotiable bills of lading, that all copies be in its possession, and that they bear no qualifying marks such as "bags torn," "contents shifting," or any other qualifications

which may impair the strength of the bill of lading. The name of the steamer and its route and destination must also be indicated.

Any irregularities are carefully considered and if they are important payment is refused and documents are returned to the beneficiary together with a notice giving reason for return. If the documents are returned to the beneficiary the fact that they have been presented and payment refused is indicated on the credit card to prevent the same documents being passed by the department subsequently without the proper changes having been made.

#### **Transmission of Documents Abroad**

If on the other hand it is established from the examination that the draft and the documents are drawn in conformity with the terms of the credit, a compended entry of the transaction is made on the credit card and the payment is deducted in order to show the amount still outstanding on the credit, if any. During the process of preparing the letter of transmittal a bookkeeping ticket debiting the foreign correspondent for the amount of the draft is prepared. After the work has been rechecked the documents together with the letter of transmittal are forwarded to the foreign correspondent, the originals by the first steamer, and the duplicates by a later one.

#### **Warehousing of Merchandise**

In some cases goods may be destined to a port to which sailings from New York City are infrequent and the goods may arrive in New York City some time before shipping accommodations can be found. The foreign applicant for the letter of credit will likely have stipulated that in a case of this sort the bank is to make advances to the exporter upon railroad bills of lading or upon warehouse receipts pending the arrangement of shipping accommodations. When a ware-

house receipt is presented it is approved by an officer, who gives it the same consideration that he would give to a similar receipt offered as collateral to secure a loan. During storage the shipper is required to furnish warehouse insurance in favor of the bank. The bank often negotiates this insurance as a service to shippers, taking out blanket policies covering all such goods stored and charging each for his portion of the premium covering his particular lot of goods. The bank also communicates with the warehouseman advising him of its interest in the merchandise and requesting that he make no delivery except upon its order. It also inquires as to the condition of the merchandise stored and requests the bailee to render bills for storage to it direct. These bills are then paid by the bank and charged to account.

It is necessary that warehouse receipts be surrendered to the shipper or his broker in order that the goods may be placed aboard ship and ocean bills of lading obtained. Pending an exchange of this sort the bank is protected by a trust receipt executed by the one who is to make the exchange. When the proper shipping documents are received the trust receipt is canceled and the documents forwarded to the foreign correspondent in the usual way.

### **Payment by Cashier's Check**

After the transaction has been found to be in order settlement is made with the customer. This settlement is effected by payment either in the form of (1) a cashier's check or credit to his account, or (2) by accepting a draft in his favor, according as the credit is a straight or an acceptance credit.

When the bank makes a payment to the beneficiary by means of a cashier's check, it immediately reimburses itself for the payment and collects its commission usually by charging the amount to the foreign correspondent's account in the "due to banks" section. The offsetting entry is a credit ticket

crediting either Cashier's Checks or the customer's account, according to the method used in settling with the beneficiary, together with a ticket crediting the Commission account for the bank's commission. Under a reimbursement credit, however, the account of the foreign correspondent is not charged, instead the method of reimbursement agreed upon is used. Usually this reimbursement is made by drawing upon the foreign bank opening the credit.

A representative of the auditing department checks the accuracy of these tickets and they are then passed either to the bookkeepers or to the check clerk of the department, depending upon whether the beneficiary's account is to be credited or he is to receive a cashier's check. The payment slip, bookkeeping tickets, and cashier's check then receive the signature of the head of the department and of a per procura-tion signer and the check is passed out to the presenter of the documents against the receipt which was given to him by the window clerk earlier in the day. Checks remaining uncalled for at the end of the day are mailed to the beneficiary. On the other hand, if the beneficiary's account has been credited for the amount of his shipment the bank sends him an advice of credit on the usual form.

When the bank makes payment by check it assures itself of reimbursement by having the foreign bookkeepers place a "hold" against the proper correspondent's account. Accordingly the payment slip is despatched to the bookkeeper for approval before the check is issued. If the payment will cause an overdraft, that fact is noted upon the payment slip before it is returned to the department. The usual search among the various departments of the bank for uncredited funds to the account of the foreign correspondent is thereupon instituted, after which the transaction is reported to an officer who may assume responsibility for approving it in spite of the overdraft.

### Payment by Acceptances

For the sake of clearness, the discussion thus far has been confined to straight credits, that is, those against which straight payments are made or immediate credit is given to the exporter. This type of credit is by far the most prevalent in the commercial credit export department for reasons already stated. There are a considerable number of acceptance credits, however, that is, those against which time drafts are drawn to be accepted by the New York bank. This acceptance constitutes in fact an immediate reimbursement to the exporter if he desires it, for he is able to discount the draft at a favorable rate in the New York discount market or sell it to the accepting bank. When called upon to accept a draft drawn under a letter of credit, the bank on the practice of which this book is based accepts it, crediting Acceptances of the National City Bank—Foreign, and debiting Customers' Liability under Acceptances of the National City Bank, for the amount of the acceptance—as explained in Chapter XIV, page 398. Acceptances of this department are entered in an acceptance register and maturities are watched by means of a tickler similar to that used in the work of the import commercial credit department. The bank does not reimburse itself from the foreign correspondent, of course, until the acceptance matures, and the liability of the foreign bank to reimburse this bank for outstanding acceptances as they mature is represented by this customers' liability account. The bank makes it a practice to send bills for commission when the draft is accepted, but in some instances it is arranged that the commission is not to be paid until maturity, hence, the Commission account is credited at the time of acceptance and a special account receivable of the customer is charged for the amount of the bill sent him. At the time of the payment this special account of the customer is credited and the commission end of the transaction is closed.

### Domestic Letters of Credit

The export commercial credit department also issues domestic letters of credit to finance domestic shipments in much the same manner that the import commercial credit department issues foreign letters of credit to finance imports from abroad. The foreign letter of credit is characterized by use of ocean bills of lading, the domestic credit by railroad bills of lading, warehouse receipts, or delivery orders. In operation they work out in the same manner and it will therefore be unnecessary to describe the domestic credits in detail.

The domestic credit is generally used to finance shipments from the interior of the country to the seaboard where railroad bills of lading are to be exchanged for ocean documents, and the shipment is sent abroad usually under a foreign letter of credit, or vice versa for imports coming into the country under import credits for shipment to the interior. An exporter located in New York City, for instance, may establish a domestic credit in favor of a manufacturer in Chicago. The latter loads his products aboard railroad cars and receives railroad ladings which he presents to the Chicago bank in conformity with the terms of the credit and is then out of the transaction. The Chicago bank forwards the documents to the New York bank which then, in return for a trust receipt, hands the railroad bills of lading to the exporter who has established the credit. When the consignment of goods arrives in New York the exporter delivers up his railroad bills of lading, takes possession of the goods, and forwards them to an ocean steamer, receiving ocean ladings in return. The exporter may be the beneficiary of a credit opened by a London importer, for example, and under this arrangement he presents the documents to the export commercial credit department and applies the proceeds to his domestic credit, which leaves him his profits without employing any of his own money in the transaction.

### Examples of Domestic Credits

Typical examples of the operation of domestic credits occur in connection with financing exports of certain steel products and imports of sugar. A New York broker may have an order from a customer located abroad calling for shipment of certain steel products which must be constructed according to specifications furnished by the buyer. To finance a purchase of this sort the buyer will quite likely provide the seller with an irrevocable credit good for, say, 12 months. On the strength of this letter of credit in his favor the broker induces his bank to open a domestic credit in favor of the manufacturer with whom he places the order for the steel goods, for a period of 9 months. Under this domestic credit the manufacturer receives payment for the steel from the bank as he delivers it in New York. The broker, who is liable under the domestic credit for reimbursement to the bank, makes the reimbursement as he places the steel aboard ship and realizes under his foreign export credit.

The use of a domestic credit in connection with the importation of sugar is the reverse of the steel transaction just outlined. Let it be supposed that on June 1, an American importer contracts to sell a local wholesaler a certain quantity of sugar for September delivery. The financing of the transaction may be done by means of a domestic commercial credit authorizing the seller to receive payment from the bank in New York as he delivers the sugar to a railway company for shipment to the purchaser. The importer then arranges for the purchase of the sugar abroad. This transaction is financed by means of a foreign import commercial credit authorizing the seller abroad to receive payment as he forwards the sugar. As shipment is made the outlays which the importer must make under the foreign import credit are met by the benefits which are accruing to him under his domestic credit.

### Advances on Export Bills

Frequently a mercantile house, which does most of its foreign business on a collection basis, finds itself in need of funds and desires to raise money on these outstanding shipments

In such a case the bank makes an advance or a loan upon the security of any collections which may be pending. The export commercial credit department handles this type of transaction by obtaining from the foreign collection export department sufficient of the applicant's collection items to cover the prospective advance, with a suitable margin. The tickets in the collection department's files covering the items pledged are stamped with a record of the fact that an advance has been made against them, so that the proceeds when received will not be paid to the exporter but retained instead to satisfy the bank's claim.

The advance is made to the borrower either in the form of a cash payment or an acceptance. Advances made in this way are debited to an account termed "Advances on Export Bills," at the time when payment is made and Cashier's Checks, the deposit account of the applicant, or the Acceptances account is credited according to the method of payment used. Complete entries of the transaction are also made in the following records: an advance book, the function of which is to record advances outstanding, a customers' liability book, the function of which is to show the liability of customers under this form of borrowing, a detailed balance book, which gives on one page a summary of all the advances to a particular customer and of the balance due from him upon these advances, and a regular credit card upon which all the details concerning each advance are given.

When customers pay these loans, entries reducing the advance account and accounting for the bank's interest and commission are made.



### Department Records

The beneficiaries', or credit, cards constitute, of course, the main record of the operations of the export commercial credit department, as has already been brought out in the course of the discussion. In addition the department keeps a number of auxiliary records which have been casually referred to.

### Contingent Liability Ledger

The contingent liability ledger is the most important of these auxiliary books and it has the function of recording all the credits issued by foreign banks and individuals and all payments made thereunder, so that the difference constitutes the contingent liability of the New York bank under export commercial credits. All the credits issued by a particular bank or individual are grouped together under one account occupying possibly several pages. These accounts are further grouped together by cities and the cities by countries, so that, for example, all the credits opened by Danish banking or non-banking concerns would be found in one section of the book, the Copenhagen banks occupying a part of that section and the account of a particular bank located in that city occupying a certain number of pages within that subdivision. This book consequently contains in a readily available form all information concerning the activities of any foreign bank, city, or country, in the opening of commercial credits with the New York bank. In fact, a weekly report of the volume of credits issued and payments made, classified as above, is prepared from this book for the use of the foreign bookkeepers and officers of the bank. All credit cards are sent to the bookkeepers who have charge of this ledger at the time the credit is opened and they enter the amount in the debit column of the proper account, indicating on the credit card that such entry has been made. Payments reducing the con-

tingent liability are posted from the payment slips to the credit of the account after payment has been made and before these slips are filed away. All canceled credits are closed out of this record so that the balance constitutes the net liability of the bank under export letters of credit.

### Expiry Tickler

An expiry tickler brings those credits which expire each day up for attention, so that they may be closed from the books, or the advice as to their disposition may be obtained from the proper parties.

The cable clerk of each section keeps a memorandum book of all charges which arise out of cables, and from this book he prepares the cable bills which he follows up until they are paid. A correspondence folder for each credit opened is also kept on file. The folder is stamped with the number of the credit, is filed numerically, and contains all correspondence and other data pertaining to a particular credit. This folder is especially for the use of the correspondents in answering inquiries and adjusting irregularities arising out of transactions under letters of credit.

### Summary of Book Entries

No daily proof is prepared by the export commercial credit department, the changes effected in the accounts are entered rather by means of debit and credit tickets. A description of the most important of these entries as made in the bank on the practice of which this book is based will serve as a summary of the work.

- 1 The Cashier's Check account is credited whenever a check is issued as payment under a commercial credit.

- 2 The Commission account is credited for all commission charges collected from customers and debited for any allowances made to guarantors.

3 The Due to Banks—Foreign accounts, representing the deposit accounts of letters of credit issued, are debited whenever payments are made under letters of credit issued by those banks

4 Customers' Liability, Acceptances of the National City Bank under Commercial Credits—Foreign represents the contingent liability which customers incur when the New York bank accepts drafts drawn under their letters of credit and therefore is debited at the time of such acceptance. The bank pays the acceptances at their maturity and at the same time it credits this contingent liability account and debits the customer direct. A similar account labeled "Domestic" instead of "Foreign" has a like function in connection with domestic letters of credit

5 Acceptances of the National City Bank under Commercial Credits—Foreign represents the direct liability which the bank incurs when it accepts drafts drawn under its foreign letters of credit. This account therefore is credited at the time of acceptance and debited when the item is paid at maturity. A similar account is kept for domestic letters of credit

6 Advanced to Customers on Export Bills represents the loans which the bank has made against the security of bills of exchange entered with the foreign collections export department for collection. This account is debited at the time of such loan and credited when the loan is liquidated

7 Advanced to Customers on Foreign Shipments, and Advanced to Customers on Domestic Shipments, are accounts which serve a function similar to the Advances to Customers on Export Bills account except that shipping documents serve as security in place of export bills

8 Interest account is credited for all charges for interest made on advances, whether against export bills, foreign shipments, or domestic shipments

## CHAPTER XVI

### LETTERS OF CREDIT AND TRAVELERS' CHECKS

#### Letters of Credit

A travelers' letter of credit (Form 73) may be defined as an instrument issued by a bank authorizing certain of its correspondents to advance funds on or before a stipulated date up to a specified amount on the demand of a designated beneficiary. The method by which the beneficiary obtains funds under a letter of credit is generally by drawing a draft on the issuing bank or upon one of its correspondents designated in the instrument and negotiating this draft with some bank located wherever the beneficiary happens to be at the time the funds are needed. The travelers' letter of credit is therefore in effect an authorization to draw drafts in instalments against the issuing bank or its designated correspondent. This form of credit is used principally by travelers to carry funds which may be needed for their journey, hence the terms "travelers' letter of credit" and "circular letter of credit" are used to distinguish them from a commercial letter of credit, or a commercial credit, used for the purpose of importing and exporting merchandise.

#### Travelers' Checks

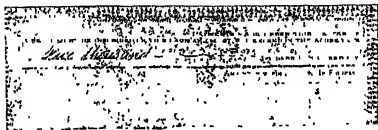
Another convenient form in which travelers may carry funds is by means of a travelers' check. A travelers' check (Form 74) is a special form of check adapted to the use of travelers. It is usually issued in denominations of \$10, \$20, \$50, and \$100, and made payable by the issuing bank or through certain of its correspondents. This form of check is signed by the owner at the time of issuance and it is validated



by the owner's signing it a second time in the presence of the one who is to cash it. The travelers' check differs from the letter of credit mainly in that it is payable as a whole, while the letter of credit is payable in instalments according to the wishes of the beneficiary. A travelers' check may be regarded as a form of bank note which is useless until it is countersigned by the owner.

### Dollar and Foreign Currency Credits

Travelers' letters of credit may be classified according to the currency in which they are issued as dollar credits and



Form 73 (b) Travelers' Letter of Credit (reverse).

foreign currency credits. A dollar credit authorizes the holder to negotiate drafts drawn in the currency of the United States while a foreign currency credit authorizes drafts to be drawn in the currency of some foreign country. Formerly pounds sterling credits were used almost exclusively by Americans traveling abroad, due to the fact that drafts drawn in that currency commanded the best rate. In recent years, however, dollar credits have assumed the ascendancy so far as the American traveler is concerned.

Travelers' checks at the time of writing are issued only in American currency. These are in normal times convertible into foreign currencies at fixed rates of exchange, but in time of violent fluctuations in the exchanges they are made con-



Form 74- Travelers' Check. (Size 9 x 3¼.)

vertible at the prevailing buying rate for bankers' sight drafts on New York in the place and at the time of cashing the check

### **Paid and Guaranteed Letters of Credit**

Letters of credit may also be classified according to the way in which the issuing bank has been paid for them. On this basis a letter of credit may either be a paid credit, a guaranteed credit, or one issued against the deposit of collateral security.

A paid credit is issued for cash or its equivalent. The cost of such a credit is the face amount of the dollar instrument or, in the case of a foreign currency credit, the dollar equivalent of the foreign currency amount converted at the current rate of exchange. To this face amount is added a commission charge of one-half of 1 per cent.

Under a guaranteed letter of credit the applicant pays the issuing bank only as the latter actually makes outlays to meet drafts drawn under the credit. Such a credit is issued upon the written guarantee of an individual, firm, corporation, or bank that drafts drawn under the credit will be paid as they are presented. The charges for a credit of this kind are the face amount of the individual drafts, plus commission at the usual rate of one-half of 1 per cent. In issuing foreign currency credits which authorize drafts to be drawn on foreign banks, the bank adds an interest charge of, say, 6 per cent for the number of days required for the draft to reach New York from the bank on which it was drawn. This charge is made to reimburse the issuing bank for loss of interest. The account of the issuing bank is charged by the foreign correspondent at the time of paying the draft. The issuing bank reimburses itself, however, by collecting from the guarantor after the draft has reached New York. The interest charge therefore is for the purpose of paying for the use of the funds between the time the New York bank makes the advance abroad for the applicant and when it is reimbursed in New



York The time involved is, of course, the mail time from the place of business of the drawee bank to New York City

### **Letter Issued Against Collateral**

Occasionally a letter of credit is issued on the basis of a deposit of collateral with the issuing bank Under these terms it is handled in much the same manner as a guaranteed credit, the reimbursement to the bank being made in a similar manner and the commission and interest charges being the same The client furnishes collateral in the form of stocks, bonds, etc., against which a loan to reimburse the bank may be made in case of necessity The bank may also find it advisable at times to segregate a portion of the balance of a customer to cover a guaranteed letter of credit.

### **Travelers Checks Issued for Cash**

A letter of credit may be paid for by the applicant either in advance or in instalments as the beneficiary avails himself of the right to draw drafts Travelers' checks, on the other hand, are always issued for cash for the reason that the Comptroller of the Currency does not sanction the inflation of the national currency which would result were travelers' checks issued on a credit basis

### **Classification of Credits**

Travelers' letters of credit may be classified according to the arrangement in effect between the issuing bank and the paying bank or banks On this basis a credit may either be a specially advised, a circular, or a clean credit

*Specially Advised Letter of Credit* A specially advised letter of credit is one addressed to only one bank Under this form of credit the beneficiary is able to secure funds from this specially advised bank only While this form of credit may be availed of at only one bank, it has the advantage

that it may be canceled readily and that payment may be stopped quickly in case the instrument is lost. A credit of this class therefore is used generally by a person who is going to remain in one place abroad.

*Circular Letter of Credit* A circular letter of credit, so far as the banks are concerned, has three parties or groups of parties—the issuing bank, the drawee bank, and the listed correspondents. Under this form of credit the beneficiary is given the option of drawing drafts upon any of the drawee banks mentioned in the letter, and these generally include one or more of the large correspondents of the issuing bank in one of the three leading foreign centers, viz., London, Paris, or Berlin. Under a dollar circular credit, however, issued by a New York bank the drafts are to be drawn upon the issuing bank itself.

The list of correspondents named in connection with a letter of credit consists of those banks which are asked to honor drafts drawn under the letter of credit, in other words, they are the agents which will cash whatever drawings the traveler may find it convenient to make, up to the capacity of the letter, of course. The names of these correspondents are recorded in a booklet, called the "List of Correspondents," which accompanies the letter of credit. During the season of heavy travel abroad, especially in Europe, the bank issues letters of credit addressed to all of its foreign correspondents numbering several thousand. A travelers' credit of this sort is termed a universal letter of credit. At other times, however, the bank obtains a list of the countries which the traveler expects to visit and it includes in the list of correspondents only those foreign banks upon which the traveler may have occasion to call for funds.

*Clean Credits* A clean credit does not require the use of a letter of credit instrument. This kind of credit is opened usually by cable or letter with only one correspondent, and

it requests the correspondent to honor sight drafts drawn by the beneficiary up to the amount of the credit. This form of credit is also very similar to a deposit account opened in a foreign bank by the American bank for the beneficiary. There is this difference, however, that in the case of a deposit the foreign bank has the use of the undrawn balance, while under the clean credit either the American bank or the applicant has the use of the money. In practice the clean credit appears in a variety of forms. It may be payable in instalments at the convenience of the beneficiary, or the payments may be restricted to a specified amount periodically. These periodical payments may be cumulative or non-cumulative.

With respect to the relations existing between the issuing bank and the paying banks, the travelers' check is very similar to a dollar circular credit in that it is drawn on the issuing bank and negotiable with all of its correspondents. No special list of correspondents accompanies the travelers' check since its very form is such as to insure its wide acceptability.

### Letter of Credit Department

The work of the letter of credit department is divided into two sections: the one having to do with letters of credit, the other with travelers' checks. The first section is further divided into two parts: (1) that which performs the necessary functions in connection with the bank's own letters of credit, and (2) that which makes payments under letters of credit issued by banks. Owing to the fact, however, that the process of issuing travelers' checks closely parallels that of issuing letters of credit, these two phases of the work will be treated together and the function of making payments under foreign credits will be dealt with subsequently. The operations performed in connection with the bank's travelers' checks and letters of credit consist of:

1. Issuing the checks and letters of credit.

- 2 Honoring them as they are presented to the bank for payment
- 3 Under guaranteed credits, reimbursing the bank for the advances which it is required to make

### Application for Letter of Credit

A client desiring to open a letter of credit is requested to fill out an application blank (Form 75) furnished by the bank. This application form states the name of the beneficiary, the amount of the credit, the expiry date, countries or cities in which the credit is to be used, and directions as to whom and how the applicant desires the letter to be sent. The applicant also agrees that in case the letter of credit is lost immediate notice to that effect will be given by telegram. The applicant agrees further that he will immediately reimburse the bank for all expenses incurred in connection therewith and for all payments made under the letter of credit before actual notice of loss is received by the agent making such payments. The application also states the method which the applicant wishes to use in paying the bank and it is signed by him. Along with the application three specimens of the beneficiary's signature are required. One of these is to be kept by the issuing bank and the other copies are to be sent to the foreign drawee banks in case the credit is to be issued in foreign currency.

Excepting in the case of applications for cash letters of credit over the counter, the application is sent to the signature department for verification of signature. Most frequently the applicant desires a guaranteed letter of credit. Under such circumstances the credit rating of the applicant enters into the transaction and a sort of offering ticket, styled an authorization slip, is submitted to the officers of the bank who are in charge of the applicant's territory. This authorization slip is passed upon in the usual way and returned to the letter

THE NATIONAL CITY BANK OF NEW YORK

Signature of beneficiary

*Joseph Jones*

THE NATIONAL CITY BANK OF NEW YORK

Signature of beneficiary

*Joseph Jones*

THE NATIONAL CITY BANK OF NEW YORK

Signature of beneficiary

*Joseph Jones*APPLICATION FOR  
LETTER OF CREDITNo. ---  
Place *Indianapolis Ind*  
and Date *July 1 1921*THE NATIONAL CITY BANK OF NEW YORK  
NEW YORK CITY

Dear Sirs

Please issue your Letter of Credit

in favor of *Mr. Joseph Jones*  
 for *five thousand (\$5000.00)* dollars  
 good until the first day of *January, 1922*  
 for use in *England, France, and Africa*  
 to be sent *Mr. Joseph Jones*  
*Hammond, Indiana*

Remarks *this letter of credit is to provide*  
*funds for Mr. Jones while making*  
*a business trip through the above*  
*countries.*

The undersigned hereby agrees that in case the said Letter of Credit or any renewal or extension thereof be either lost or stolen immediate notice thereof shall be given you by telegraph, and in case of such loss or theft the undersigned hereby authorizes you to take such precautions as you may deem advisable for the prevention of fraud and agrees to provide immediate reimbursement for all expenses in connection therewith and for all payments made in reliance upon the said Letter of Credit, before actual notice of the loss thereof shall have been received by the person making such payments.

In reimbursement of all payments made under the above requested Letter of Credit, together with your usual charges, you will please

(\*) *find check enclosed*

Yours very truly,

*First National Bank*  
*of Indianapolis*  
*John Doe President*

(\*) Please insert one of the following instructions:  
 (1) *Pay check enclosed.*  
 (2) *Draw on account with your usual register of date.*  
 (3) *Send to destination for cash.*

of credit department as authority for issuing the letter. Should the applicant pay cash for the letter of credit the same style of authorization slip is prepared for the purpose of obtaining a record, but since the credit rating of the applicant does not enter into the transaction it is unnecessary to have the approval of the officers

### **Issuance of Letter of Credit**

After the application has been approved the letter of credit instrument is drawn up. This process consists merely in filling in upon a numbered form letter such data as the amount of the credit, the date of issue of the letter, the expiry date, which is usually one year from the date of issue, and the name of the beneficiary. This form letter is printed on erasure-proof paper. As an added protection against alteration of the letter, all written matter is underlined so that any attempt to make alterations would be discovered. The signatures of two officers of the bank are required to make the instrument valid.

### **List of Correspondents**

Accompanying the letter of credit is the list previously referred to containing the names of the paying agent banks in every city of importance throughout the world. The drafts are not to be drawn against the paying agents, these banks have only agreed to make payments or honor drafts drawn in accordance with the terms of the letter of credit and to reimburse themselves as directed on its face. In order that the correspondents may determine the genuineness of letters of credit presented to them, the issuing bank lodges with them samples of its letters of credit together with specimen signatures of those authorized to sign them for the bank.

The list of correspondents contains complete instructions for guidance of the owner in using the letter of credit. In addition it contains a specimen of the holder's signature which

constitutes his means of identification. By means of the signatures of the officers of the bank appearing on the instrument itself, and the signature of the holder, the paying agent is enabled to assure itself that all is in order before it makes payment. There is a form of letter of credit used by some banks and bankers on which the signature of the beneficiary appears on the instrument itself. By making the list of correspondents containing the owner's signature a separate instrument, however, and by instructing the beneficiary to carry the list separate from the letter of credit, both of which must necessarily be presented at the window of the paying agent when drawings are made against the letter of credit, the chances of funds falling into the hands of unauthorized persons are reduced to a minimum. If the beneficiary loses either the booklet containing the list of correspondents or the letter of credit itself it is worthless to the finder.

### Guaranteed Credit

The applicant for a guaranteed credit is required to sign a guarantee in which he engages to reimburse the bank for all drafts drawn upon it under the letter of credit, including the usual commission charge of  $\frac{1}{2}$  per cent on the face amount of the drafts, and an interest charge of 6 per cent for the mail time between the city of the drawee bank and that of the issuing bank in the case of foreign currency drafts. The guarantee of reimbursement is worded as follows

In consideration of the issuance by The National City Bank of New York, at our request, of its Letter of Credit No ... .., in favor of. ..  
 ... ..  
 for . . . . .  
 receipt of which is hereby acknowledged, the undersigned agrees to pay on demand after date to The National City Bank of New York, the amount of all drafts or other evidences of disbursements of funds under the above described

Letter of Credit if drawn in Dollars, or the Dollar Equivalent at the rate fixed by The National City Bank of New York, if drawn in Foreign Currencies, and commission charges of . . . per cent, and interest for . . . days at the rate of . . . per cent per annum All amounts so paid by the undersigned shall constitute part payment of this obligation

In the case of a paid letter of credit the guarantee is of course dispensed with The bank receives cash and it credits the amount to an account termed Paid Letters of Credit This is a liability account the balance of which represents the bank's obligation to meet drafts drawn against funds which it has received It therefore has the same status as a demand deposit account, and on the condensed statement of the bank this and other similar items are combined with actual amounts due depositors on account to form the demand deposits

### **Issuance of Travelers' Checks**

The issuance of travelers' checks to clients who call for them at the bank is always a cash transaction, hence the purchaser is merely requested to fill out a signed order specifying the amounts and denominations of checks desired The owner is requested to place his signature in the upper left-hand corner of each check immediately as a protection in case the checks are lost At the time of cashing the checks he is required to sign a second time in the lower left-hand corner, the similarity in the two signatures constitutes his identification The cash obtained by the bank from the sale is the face value of the checks plus a commission charge of one-half of 1 per cent The amount of commission is credited to the Commission account and the face amount of the check to Travelers' Check account This account is a liability account representing the obligation of the bank to meet checks outstanding, just as is the Cashier's Check account or the Circulation account



### Interior Correspondents' Travelers' Checks and Letters of Credit

The small demand made upon many banks for travelers' checks and letters of credit does not make it practicable for them to maintain their own letter of credit department and to issue their own forms. To enable these banks to supply this demand their metropolitan correspondent extends to them its facilities for issuing letters of credit. Under this system the city correspondent sends the country banks a supply of its travelers' checks and letters of credit which they hold under a trust receipt. These letters of credit are already signed, numbered, and stamped with a limit amount for which they may be drawn. Common limits are \$1,000, \$2,500, and \$5,000. Since the blank instruments are already signed the object of such limitation is to prevent those who might obtain the blank letters fraudulently from drawing excessive amounts.

When a country bank issues one of these letters of credit it advises the city correspondent of the fact, using the correspondent's special form for the purpose, and it also sends specimen signatures of the beneficiary together with its guarantee and a check or instructions to charge its account for the amount of the letter of credit. Country banks issue these letters of credit for cash or against guarantee. The city correspondent bank usually allows them one-half of the commission charged.

When making a sale of travelers' checks the country bank requests the purchaser to sign a form of application (Form 76) which it sends to its city correspondent as an advice of the sale. This advice contains the name of the bank making the sale, the name of the purchaser, the numbers appearing on the checks sold, and a remittance for the amount of the sale. This remittance may take the form of funds enclosed with the advice or of instructions to charge the account of the country bank. The amount involved in the settlement

THIS WILL \_\_\_\_\_ No. \_\_\_\_\_

PURCHASER'S APPLICATION FOR  
TRAVELERS' CHECKS  
OF  
THE NATIONAL CITY BANK OF NEW YORK

SOLD BY First National Bank  
Indianapolis Indiana

FOR USE IN England and France (STATE IF IN FOREIGN COUNTRIES)  
(CANADA OR UNITED STATES)

QUANTITY	DENOMINATION	AMOUNT	CHECKS NUMBERED	
			FROM	TO INCLUSIVE
10	\$10	\$ 100 <sup>00</sup>	4275	4287
	\$20	\$		
5	\$50	\$ 250 <sup>00</sup>	7981	7985
5	\$100	\$ 500 <sup>00</sup>	10654	10658
	TOTAL	\$ 850 <sup>00</sup>		

SIGNATURE OF PURCHASER B. Ralph Moore

RESIDENCE OR BUSINESS ADDRESS 75 Main St.

TOWN OR CITY Indianapolis STATE Indiana

ENCLOSED FINE DRAFT FOR \$ 850<sup>00</sup>  
~~YOUR ACCOUNT HAS CREDIT FOR~~

To THE NATIONAL CITY BANK  
OF NEW YORK  
65 WALL STREET  
NEW YORK

CASHIER OR TREASURER John Doe

DATE July 1 1921

PLEASE SEND US:

\_\_\_\_\_ BOOKS OF \$10 CHECKS \_\_\_\_\_ BOOKS OF \$50 CHECKS

\_\_\_\_\_ \$20 " \_\_\_\_\_ " \$100 "

(EACH BOOK CONTAINS 10 CHECKS)

between the two banks is the face amount of the checks sold, since the city correspondent permits the country bank to retain the usual commission of  $\frac{1}{2}$  per cent as its profit from the transaction. The former bank obtains its profit in the form of the interest from using the funds involved in the face amounts of the checks from the time it receives such funds from the seller bank until the checks are paid.

Instead of delivering travelers' checks and letters of credit to applicants, country banks often refer clients of theirs desiring to purchase such instruments direct to their city correspondent. In such cases the country bank usually gives the applicant a letter of introduction to the city correspondent and it undertakes to guarantee payments under a letter of credit if such is issued. The bank issues such instruments in the usual way for direct applications. For bringing business to it in this manner, the issuing bank allows the country bank one-half the commission charge involved in the transaction.

### Advices to Drawee Banks

Inasmuch as foreign currency credits require that drafts be drawn on foreign drawee banks, it becomes necessary for the bank issuing the credit to advise the foreign banks of the issuance of such letters of credit in order that they may have sufficient information on hand to honor these drafts as they are received. In most cases the bank draws foreign currency credits upon a certain few of the largest English, French, and German banks, and it advises these banks periodically of the issuance of letters of credit upon which they may expect drawings, giving such details as the number of the credit, the date it was drawn, the amount, specimen signatures of the beneficiary, and date of expiration. It is the custom for foreign banks to acknowledge the receipt of these advices by means of form letters which contain about the same information as the original advices.

### Illustrations of Use

The use of a letter of credit may be illustrated by a typical example. Suppose a traveler holding one of the National City Bank's dollar letters of credit needs funds when he has reached, say, Naples. The correspondent in that city as named in the list of correspondents is the Banca Commercial Italiana. The traveler presents the letter at that bank and asks payment of \$100. The Italian banker prepares a draft for \$100 drawn on the New York bank and has the beneficiary sign it. The traveler writes his signature in the presence of an officer who compares it with the one on the list of correspondents. If found to agree, the Italian banker pays the equivalent of \$100 in Italian currency at the prevailing rate for sight drafts on New York and makes a record of such payment on the reverse side of the instrument. The reverse side of a letter of credit thus always shows the balance remaining undrawn under the letter. The draft states that it is drawn against letter of credit No . . . of the National City Bank of New York and it is sent by the Italian bank to its correspondent in New York, or more likely to the National City Bank itself for collection and credit.

In case the credit is issued in pounds sterling and the traveler asks for £100, the Italian bank prepares the draft for this amount to its order drawn on the reimbursing London bank named in the credit, paying the traveler in Italian money the equivalent of £100, at the rate prevailing for sight drafts on London. The Italian bank sends the draft to its London correspondent for collection and credit. The London bank compares it with the information and signature which it received from the National City Bank at the time the letter of credit was issued and if all is in order it pays the draft, charging the account of that bank. The London bank prepares a debit advice covering the amount of the draft and sends it to New York. At intervals the London bank forwards

the paid vouchers to the National City Bank as evidence of payments

While a letter of credit will only be honored, as a general rule, by the correspondents named in the list which accompanies it, travelers' checks may be freely negotiated anywhere. They are readily accepted by banks, hotels, railroads, and business houses generally throughout the world. At the time of purchasing the checks the owner signs them in the upper left-hand corner. When he wishes to cash one of them he again signs the check in the lower left-hand corner in the presence of the person by whom the check is to be paid. That person is thereby enabled to authenticate the signature and to determine whether it will be safe for him to advance funds. For this reason the counter-signature should not be placed upon the check until the owner wishes to use it, and then only in the presence of the person honoring the same. As has already been stated, under normal conditions in the foreign exchange market travelers' checks are cashed abroad at fixed rates of exchange, but in time of violent fluctuations in the exchange rates, such as have prevailed in recent years, they are made convertible at the current buying rate for bankers' sight dollar drafts on New York.

### **Expired and Exhausted Credits**

In case the draft exhausts the letter of credit the foreign bank requests the beneficiary to surrender the instrument and forwards it, attached to the draft, to the New York bank where the letter is filed for record. Periodically the letter of credit department traces all outstanding guaranteed credits which have expired. As these instruments are returned they are marked canceled and retained in the department's files.

A request for the extension of the period of validity of a letter of credit is treated in the same manner as if a new credit were to be issued. The client is required to sign applica-

tion and obligation forms which are passed upon in the usual manner and when approved a letter of extension is given. This letter of extension is to be presented in conjunction with the letter of credit when it is desired to obtain funds under it.

### Lost Letters of Credit and Travelers' Checks

When a traveler loses a letter of credit the directions given in the list of correspondents are followed. The procedure varies with the type of letter involved, but rather expensive cable messages between the beneficiary and the issuing bank, between the issuing bank and correspondents, etc., are always necessary. The issuing bank, however, endeavors to reduce the cost of stopping payment as much as is possible by sending stop-orders by cable to such points only where the letter is likely to be promptly presented for payment and communicates the order to other banks by mail. The cost of stopping payment under a letter of credit, is nevertheless considerable, say from \$50 to \$75, the more nearly universal the letter, the higher the cost.

When a person loses a travelers' check he notifies the issuing bank or the country bank through which the check was purchased, making application for reimbursement for the amount lost. The issuing bank has the loser sign a bond of indemnity under which he agrees to indemnify the issuing bank for any loss which it may incur through being obliged to pay the lost check. As surety, the owner of the lost check obtains the signature of another responsible party. The country bank which sold the check, if sale was made in that way, also signs the bond of indemnity to attest to the credit rating of both the other signatories. On the security of this bond, the face amount of the lost check is returned to the owner. From this point stop-payment is handled as in the case of an ordinary check. Should the travelers' check be presented for payment the bank refuses to honor it and traces the transaction to the

one who paid the check without exercising due diligence. Recovery of the amount is then obtained from this person.

### Honoring Travelers' Checks and Drafts

Drafts drawn under letters of credit come to the bank from abroad in the usual way for foreign collections and deposits. The receiving departments of the bank send these incoming items to the letter of credit department which compares them with its records and, having found them to be drawn in the proper manner, makes the proper bookkeeping entries.

If the drafts are drawn under a paid letter of credit the amount is charged to the Cash Letters of Credit account, thereby reducing the bank's liability under these instruments. If the draft is drawn under a guaranteed credit, however, the guarantor is to pay the amount at this time. The customer is either sent a bill for the face of the draft plus interest and commission charges, or an advice of debit, in case the guarantor has an account with the bank and this account is to be charged. The bill and the advice of debit are both drawn in duplicate, the carbon copy serving as the bookkeeping ticket. Advances of this sort are charged to an account termed "Advances to Customers on Travelers' Letters of Credit." When the guarantor remits this account is credited for the amount paid.

Travelers' checks return to the bank either by direct sending from out-of-town banks or foreign correspondents, or through the clearing house. In either case they are received by the check desk and are forwarded to the letter of credit department for authentication. The clerks compare the signatures appearing on the checks and refer to their records to ascertain that the checks were issued in the proper manner. The checks having been found to be in order, a bookkeeping ticket is made out at the end of each day debiting the Travelers' Check account for the total of the checks paid.

## Credit Cards and Files

All the necessary information pertaining to a particular credit is contained upon the credit card shown in Form 77. At the time a credit is drawn the number of the credit, the

<b>N C B Letter of Credit</b>						
Number <u>5476</u>		Beneficiary <u>F. Cartright Evans</u>			Amount <u>\$5,000<sup><u>00</u></sup></u>	
Date <u>July 1 1921</u>						
Guaranteed by <input checked="" type="checkbox"/> Held in trust by <input type="checkbox"/>		Term <u>Sixth</u>		Expires <u>January 1 1922</u>		
<u>First National Bank</u>		Limited to _____		Continued until <u>July 11, 1921</u>		
<u>Indianapolis, Indiana</u>				* Advised ahead _____		
Signature of beneficiary _____  <u>Johansen &amp; O'Malley</u>		To be used in <u>World</u>		Cash find <u>July 12, 1921</u>		
Remarks: * Advised in _____ _____ _____ _____ _____						
Date of Debt	Represented by	Paid by N. C. B.	Payment (amount)	Amount	Balance	
<u>July 16</u>	<u>Pennock Loan Trust Co. Pres</u>	<u>July 26</u>	<u>\$11 No 8</u>	<u>500 -</u>	<u>4,500 -</u>	
Balance carried forward						



trust receipt, credit cards are prepared in a way to show that the letter forms are held in trust. Later on when advice that a credit has been issued is received, the credit card is completed. Thereafter such cards are handled in the usual way.

The letter of credit card files are composed of the following sections.

1. Clean credits, filed numerically
2. Cash and guaranteed credits, also filed numerically
3. Letters of credit held by interior banks against trust receipt, filed alphabetically by names of banks, each bank having one card showing its total holdings
4. Letters of credit held against trust receipts (in this section each individual credit has a card as described in the preceding paragraph)
5. Letters of credit sold by branches of the bank
6. Index of credits by guarantors filed alphabetically
7. A card index of all credits filed alphabetically by names of beneficiaries.

### Cash Journal

The cash journal is used to record all sales of paid letters of credit as well as all payments made by the bank on the individual drafts drawn thereunder. It therefore shows the condition of the Cash Letters of Credit account. At the time of sale of a paid letter of credit, entry is made in the journal for the amount of cash received and when drafts drawn on the bank under a letter of credit are received a charge entry is made. The balance therefore shows the amount of funds obtained from the sale of letters of credit and of which the bank has full use.

### List Book and Balance Book

In the case of guaranteed credits two books are kept: a journal called a list book, and a balance book which contains

entries to the account termed "Advances to Customers on Travelers' Letters of Credit." When guaranteed credits are issued no funds are received, as has already been stated. When the bank honors drafts drawn under such guaranteed credits, therefore, it, in effect, makes advances to customers to a corresponding amount. It remains for the bank to collect these funds. The purpose of the list book is accordingly to keep a record of such collections. In case the guarantor has an account with the bank and desires to settle the amounts of drafts paid by having the bank charge his account, the entry is made in a column labeled "Charge Account" or "Correspondent" and a statement of the debit or notice of the amount due is sent to the customer. In case the guarantor has no account or does not desire this account to be charged in settlement of drafts paid, the entry is made in a column labeled "Suspense Account," which represents "Advances to Customers on Travelers' Letters of Credit." The guarantor in this case receives a bill for the draft plus all charges and usually makes a remittance by check. When the check is received a credit entry is made to the Suspense account. The balance book contains merely a record of the daily total of the entries contained in the list book and therefore shows the status of the account "Advanced to Customers on Travelers' Letters of Credit."

### Departmental Records

The records for travelers' checks consist of a register, a cash book, and a trust receipt book.

The travelers' check register is composed of several volumes, one or more for each denomination issued. In this book each check is listed serially according to the number appearing on the check. A description of each check is given, i. e., the name of the interior bank through which the sale was made—if the check was issued in that way—the date of each

sale, the name of the person purchasing the check, the date on which the check returned to the issuing bank—this latter entry serving to cancel the check from the register—and the auditor's stamp showing that the transaction has been properly entered

The cash book shows all sales of travelers' checks, whether made by the bank itself or through its correspondents, together with the commission. This book therefore shows the status of the Travelers' Check account, which represents the amount of funds obtained from the sale of travelers' checks and of which the bank has full use

The trust receipt book shows the amount of travelers' checks held in stock by each correspondent bank.

### Payments Opened by Foreign Banks

Foreign banks issue travelers' credits in essentially the same forms as a New York bank and the New York bank makes payment under these credits in a manner similar to that cited in the example of the Italian banker making advances to the American travelers

Under a foreign circular letter of credit the bank frequently has not received advice of the issuance of the particular credit which the beneficiary presents in order to obtain funds. The procedure in making a payment under a credit of this sort consists first in ascertaining that the credit instrument is in order by having the official signature appearing thereon verified by the signature department and noting the expiration date, etc., of the credit. The beneficiary then is requested to sign drafts in duplicate drawn on the foreign bank which issued the credit. This signature having been found to agree with the registered signature which accompanies the letter of credit, the draft is sent to the foreign discount department where it is purchased at the rate prevailing for that particular foreign currency. The bank reimburses itself by forwarding the

draft to the drawee bank abroad for collection in the usual manner

More usually, however, the foreign credit is an advised credit concerning which complete instructions are on file. When such a credit is presented the beneficiary is requested to sign quadruplicate receipts, the original and duplicate to be sent to the issuing bank abroad by separate mails with an advice of debit, the triplicate to be filed in the foreign files of the bank, and the quadruplicate to be retained as an office copy. The signatures on the receipts are compared with the specimen on file and if found correct, tickets are prepared charging the account of the foreign bank and crediting cash. The payment is indorsed on the back of the letter of credit which is returned to the beneficiary, unless the drawing exhausts the credit, in which case the instrument is taken up and forwarded to the foreign bank.

It frequently happens that applications for payments are received by mail direct from the beneficiary or through a correspondent bank. Usually the letter of credit itself accompanies such a request for payment. The instrument is examined as before, a check for the desired amount is drawn, and the letter of credit, properly indorsed, is returned together with the check and receipt forms to the applicant or to the correspondent bank. The beneficiary or the correspondent bank executes the receipts and returns them to the paying bank, which forwards them abroad in the usual manner.

Foreign clean credits, under which the bank acts as paying agent, are handled in various ways. The payment may be made in the manner just described or the instructions may be to pay the beneficiary periodically. A tickler file is kept for the purpose of bringing payments to attention at the proper time. In making these payments either a cashier's check is drawn or the account of the beneficiary is credited. The payment may be made through an interior bank either by forward-

ing a cashier's check in its care or by instructing it to pay the beneficiary out of its own funds and to charge the account of the New York bank authorizing the payment

As advice of the opening of a credit by a foreign bank is received the essential details of the credit are recorded upon beneficiary's card which is similar in purpose to that of the letter of credit cards kept by the letter of credit issuing section. Entries are also made upon the card of the foreign bank, called the "guarantor's card," which shows the total number and amount of credits opened by that bank. For ready reference a card index is kept of all credits by names of beneficiaries.

## CHAPTER XVII

### FOREIGN DRAFTS, LETTER AND CABLE TRANSFERS

#### Methods of Transfer

An important part of the foreign work of a bank consists in handling transfers of funds from this to foreign countries and vice versa. Ordinarily if funds are to be transferred through a bank one of the following methods is used.

- 1 Bankers' demand or sight drafts or checks
- 2 Letter transfers
- 3 Cable transfers
- 4 Bankers' long bills

#### 1. Bankers' Demand

The bankers' demand or sight draft or check is the foreign counterpart of the domestic bank draft. It may be defined as a check payable at sight or on demand, drawn by a bank in this country upon a foreign bank with which it has a deposit account, or at least with which it has made arrangements for the draft to be honored. The draft is delivered to the purchaser who sends it to the payee. The payee cashes the draft with his bank as he would an ordinary check.

#### 2. Letter Transfers

The foreign letter transfer consists of a letter addressed to a foreign bank requesting it to make payment to the beneficiary, against receipt and identification usually, and to charge the amount paid to the account of the sending bank. By this method the purchaser of the transfer merely obtains a receipt

for the purchase price and the burden of getting into contact with the payee rests with the two banks

So far as the rate of exchange is concerned drafts and letter transfers are on an equality since both are sold at the sight rate of exchange. The letter transfer has an advantage over the foreign draft in some cases in that it is non-negotiable and less likely to be lost in transit. Again, if a letter transfer fails to reach its destination it is an easy matter to issue a duplicate, while if a draft is lost the bank must require indemnity bonds before issuing another. This disadvantage is offset to an extent by the bank's practice of drawing drafts in duplicate and delivering only the original to the purchaser. If this original fails to reach the payee, the bank delivers the duplicate to the purchaser. Should the duplicate reach the payee it will be cashed by the drawee since it is the custom in international banking to honor either the original or the duplicate, whichever is presented first. The drawee bank is responsible for avoiding paying both copies.

The draft may sometimes prove a quicker method, for if the funds are sent by draft the payee receives his draft directly from the remitter and he will presumably cash or negotiate it immediately, while if funds are sent by letter the burden of locating the payee rests on the foreign bank, and considerable time may be consumed in getting in touch with him and making the payment.

### 3. Cable Transfers

A cable transfer consists of a cable message sent by a bank in this country ordering a bank in another country to make some form of payment to a designated payee. The cable transfer has certain obvious advantages over other methods of transferring funds. In the first place it is a quicker means of transfer and would therefore be the only possible method for transferring funds in an emergency or upon short

notice Even though the remitter has sufficient time at his disposal to permit him to use a letter or draft, by electing to use a cable transfer he may have the use of his funds during the time they would have been in transit had he sent a draft or a letter payment, thereby offsetting the added cost of the cable transfer, at the same time he may watch developments in the foreign exchange market and take advantage of any favorable fluctuations up to a day or two before the remittance is due abroad

Cables are sold at the cable rate of exchange plus the charge for sending the message and of course cost more than drafts and letter payments since the banks do not have the use of the customer's funds during any appreciable time in transit and since cable fees are higher than postage Yet, for large amounts especially, the cable transfer is usually preferred. Besides those cable transfers which the bank makes for its customers, it uses this method in making transfers of its own funds necessitated by foreign exchange trading

#### **4 Bankers' Long Bills**

Bankers' long bills are time drafts, usually 60 or 90 days, drawn by one banker upon another Long bills are sold at a lower rate than sight or cable exchange, hence this form of remittance is useful in case the debtor has idle funds and wishes to anticipate payment of his debt due abroad

An example will serve to make clear the use of a long bill for making remittance to a foreign country Let it be supposed that an American importer owes £10,000 payable in London 90 days hence What form the debtor's remittance takes is immaterial to the creditor provided he receives the proper number of pounds sterling on the due date Assuming the debtor has funds on hand, he may purchase and send his creditor (1) a 90-day bankers' bill now, (2) a 60-day bankers' bill within the next 30 days, (3) a check or a letter transfer



within the next 75 days, or (4) a cable transfer within the next 90 days

Let it be assumed that the selling quotation for the day for checks is \$3 71 and for 90-day bankers' bills \$3 63¼, with corresponding rates for 60-day bills and cables. The debtor can purchase a 90-day bill for  $10,000 \times 3\ 63\frac{1}{4}$ , or \$36,325, and a check for  $10,000 \times 3\ 71$  or \$37,100, making a difference in cost of \$775 in favor of the 90-day bill. This would be recognized by the experienced user of exchange as an abnormally favorable rate for the 90-day bill.

If in the debtor's opinion there is little probability that exchange rates will move materially in either direction in the next 90 days his choice will be based on interest rates. By paying \$36,325 for a 90-day bill he saves \$775 over what he must pay for a demand bill at the end of 75 days, or, in other words, his return on an investment of \$36,325 for 75 days is \$775, or at the rate of approximately 10¼ per cent per annum. Unless the remitter has use for these funds in some enterprise which will yield him better than at the rate of 10¼ per cent within the next 75 days, obviously it would be to his interest to purchase and remit a 90-day bill.

Thus far the illustration has left out of consideration fluctuations of exchange rates, but exchange rates do not as a rule remain stationary for so long a period as 90 days. The remitter must take into consideration the fact that if he is facing a period of rising exchange rates the 90-day bill becomes a still more attractive purchase, while if exchange rates are to fall materially it will be better for him to use his funds elsewhere and to purchase a 60-day bill, demand exchange, or cable transfer later on.

### Foreign Teller's Department

The work of selling transfers of these kinds as well as that of making payments on orders from abroad, except cashing

foreign drafts, is performed by the foreign teller's department. In addition this department buys and sells foreign money as a service for customers, receives foreign deposits (see page 40), and handles foreign exchange contracts entered into by the traders of the bank.

Foreign drafts and transfers may be drawn either in foreign currency or in dollars depending largely upon what country the draft is to be drawn on. Foreign currency items are more prevalent since if drawn in the currency of the drawee's country they eliminate uncertainties on the part of the payee as to conversion rates and at the same time the selling bank has the benefit of the moderate but quick profit which comes from a sale of foreign exchange.

When a foreign draft is drawn in dollars, however, the drawer bank makes provision for insuring the payee the most favorable rate for cashing the draft by stamping on the face of the draft, "Payable at buying rate in (metropolis of the payee's country) for sight drafts on New York." Thus in any city of Argentina a dollar draft would be convertible into local currency at the buying rate in Buenos Aires for bankers' drafts on New York.

### Exchange Purchases

Applications to purchase drafts and transfers may come over the window, by mail, by telegraph, or by cable. The last two media are often used in ordering cable transfers especially. The client requesting the bank by mail or in person to issue a foreign draft or transfer fills out an application form giving his name and address, the name and address of the foreign payee, and the amount and kind of currency, so that in all cases the bank may be guided by complete written instructions. Usually the request is accomplished by a remittance covering the amount or instructions to debit the applicant's account. Letters, telegrams, and cable messages request-

ing that the applicant's account be debited for the cost are verified by examination of the signature or test word. If the remitter is not a depositor of the bank he is required to provide payment in the form of a certified check or in cash.

Many of the sales of drafts, letters, and cable transfers arise from the trading activities of the bank. The traders purchase large blocks of exchange from brokers and other dealers in the open market. Transactions of this sort come to the tellers in the form of contracts drawn up in the traders' department.

Many of the traders' contracts are effected through brokers who act as agents of the bank and receive a fixed rate of commission for making the sale. In handling a brokerage contract the broker's commission is noted on the contract form by the traders. This amount is charged to the Brokerage account and credited to the account of the broker.

Foreign exchange contracts may be for regular or for future delivery. Contracts sold for future delivery are recorded by the traders upon a card index arranged both alphabetically and by maturity dates. Contracts for future delivery may be made for delivery on a fixed date or for delivery within a certain period either sellers' option or buyers' option. In most cases the purchasers pay for exchange contracted for on delivery but it is a custom in dealing with the largest and best known dealers in the city to deliver the exchange a day or so before the sailing date of the steamer on which it will be mailed and to defer payment until the sailing day. If the contract is not fully availed of on the expiry date the customer is required to draw out the remainder or to obtain an extension from the traders, since the bank has been obliged to provide cover for it.

Remittances received in cover of drafts and transfers are credited temporarily to an account entitled "Prepaid Exchange" in order that there may be no delay in collecting

checks offered in payment When the draft or transfer is drawn the cost is debited to this account In case the applicant has made arrangements to pay cash on delivery of the exchange by messenger the cost is charged to an account termed "Unpaid Exchange" pending return of the messenger with funds This account is also used to cover the interval of time between delivery of exchange sold on contract and payment therefor

Foreign drafts and transfers are sold both for profit and as a service to customers, hence others than depositors of the bank make use of the bank's facilities for issuing these instruments These facilities, however, are not made accessible for all classes of transactions Each transaction is passed upon by someone in authority who takes care that the transaction is not made for speculation

### Cost of Drafts and Transfers

Foreign dollar items drawn on branches of the bank, which class includes practically all dollar drafts and transfers which the bank draws, cost only the face value Whatever profit the bank makes on these comes from converting the items at the branches if the payees cash them there If dollar drafts and transfers are drawn on other than branch banks the bank charges a moderate commission

For drawing a foreign currency item no commission is charged, the cost is expressed in dollars, obtained by converting the face amount at the selling rate Rates of conversion for foreign currency drafts and transfers are fixed by the traders of the bank Individual quotations are made for each large item, but rate sheets showing rates for small ones are furnished to the tellers These rate sheets are changed as often as the exchange market moves sufficiently to warrant such action By means of a weekly list showing what correspondents are to be drawn upon, the traders also control the selection of drawee banks for all foreign currency items

### Preparing Foreign Drafts

To save time and effort every instrument needed for the bank's records, the statement to the purchaser, the advices for the foreign drawee bank, and the original and duplicate drafts, are made in the same operation. Every precaution is taken to make sure the bank follows the laws and customs relating to drafts in foreign countries. For example, drafts drawn on British banks are crossed in conformity with the British custom of indicating by cross-marks across the check that it is payable only through a bank. If the checks were not crossed the privilege of having the payee identified would be denied. The original draft is delivered to the purchaser while the duplicate is filed and in case of loss of the original it is delivered to the purchaser who sends it abroad to replace the lost copy.

Attached to the draft form is a statement of the transaction, which the bank always sends the customer. Another stub serves as an accountant's memorandum for use in auditing the issuance of drafts. Triplicate copies of the draft are filed as a record of the transaction. One set is filed according to names of purchasers, the other according to payees.

Two advices that drafts have been drawn are always sent to foreign drawee banks by separate mail steamers. These are prepared on sheets underlying the original and duplicate copies of the draft. The importance of these advices cannot be overestimated since in most cases they become the basis upon which the foreign bank charges the account of the American drawer bank. The custom in international business, except in dealings with a few countries or with banks which have made other arrangements, is for the drawee bank to charge the account of the drawer at the time of the receipt of the advice rather than on the date of payment. As a general rule also a foreign bank will have been instructed by the drawer to decline to pay drafts for which it has received no advice until it has communicated with the drawer by cable and obtained its in-

structions to pay the instrument. Thus it is highly important that the bank send out its advice immediately after the draft is drawn.

The method of handling remittances received to cover the costs has already been described. If the applicant's account is to be charged the charge ticket is prepared concurrently with the draft sheets. The offsetting entry for a foreign currency draft consists of a credit to the bank's account maintained with the drawee. For dollar drafts the entry consists of a credit to the drawee bank's dollar account for the face amount, and if commission has been charged, the amount is credited to the Foreign Exchange Commission account.

### Letter Payments and Cable Transfers

In a similar way the advices, tickets, and letters used with a letter transfer are prepared. Instead of duplicate drafts and advices, a letter drawn in duplicate (Form 78) is sent to the foreign bank which is to make payment. The original of the letter is sent by one steamer and the duplicate by another.

As in the case of drafts and letters all the advices and tickets needed in connection with a cable transfer are prepared at one operation. First there is a statement for the customer (Form 79), serving as an advice as well as a receipt for the amount by him, and giving the details of the transaction. In case the cable payment does not reach the payee abroad, the conditions of sale are that refund to the purchaser shall be made at the rate of exchange which prevails on the day refund is made. To bring this condition of the sale to the knowledge of the purchaser the statement contains the following notice.

As exchange will be promptly purchased to cover this remittance, the National City Bank of New York will not be liable, in the event that payment for any reason cannot

**THE NATIONAL CITY BANK OF NEW YORK**  
FOREIGN TELLERS

ORIGINAL NEW YORK Sept 16 1921

TO National City Bank  
Bogota, Colombia NO D. 1898

Kindly make the following payments to our debt, upon identification, and against receipts to dupli-  
cate to be forwarded to us. TOTAL \$ 5,000.00

NUMBER	BENEFICIARY	ORDERED BY	DESCRIPTION	AMOUNT
7467	M M Muller	R W Wylie	same	5000

THE NATIONAL CITY BANK OF NEW YORK  
John Doe ac  
John Roe PP

Form 78 Foreign Payment Letter (Size 8 x 6)

**THE NATIONAL CITY BANK OF NEW YORK**  
FOREIGN TELLERS

No. A 777

**STATEMENT OF CABLE TRANSFER SOLD**

TERMS CASH OR CERTIFIED CHECK NEW YORK Sept 17 1921

SOLD TO Mr John Smith

ADDRESS 601 Wall St. New York N. Y.

PAYMENT WILL BE EFFECTED THROUGH National City Bank  
London, England

AMOUNT £1000/6/0 \$3.51 3.510 00

PAYABLE TO Mr Thomas J. Smith COST OF CABLE 4 13

ADDRESS 29 Exchange Place, London, E.C. TOTAL 3.514 13

ACCOUNT OF RECEIVED 3.514 13

CUSTOMERS' EXPENSE FUND CABLES				ACCOUNTS RECEIVABLE			
CHARGED		CREDITED		CHARGED		CREDITED	
DATE	TICKET NO.	DATE	TICKET NO.	DATE	TICKET NO.	DATE	TICKET NO.

BALANCE DUE

IMPORTANT NOTICES

An exchange will be promptly procured to cover this certificate. The N. C. City Bank of New York will not be liable in the event that payment for any transfer cannot be made for any amount in excess of the value in New York of such exchange at the time stated is asked. Funds are accepted only upon cash realization.

In view of the present disturbed world conditions the National City Bank of New York assumes no responsibility for errors, omissions, misregistrations, or delays in transmission or delivery of Cable Messages caused by operators beyond its control.

Form 79 Cable Transfer (Size 8 x 6)

be made, for any amount in excess of the value in New York of such exchange at the time refund is asked. Funds are accepted only upon that condition.

The second advice constitutes a confirmation of the cable, which is to be sent to the paying bank abroad. The third copy is for the use of the telegraph and cable department in preparing the message and in accounting for the charges in sending it. Three other copies of the statement constitute file copies, the first is an office record, the second is for the information of the officer who is in charge of the territory of the applicant.

### **Long-Time Bills**

Long-time bills are handled in much the same manner as sight drafts except that at the time of issue a credit is passed to a Long Bills account. When advice is received from abroad that such bills have been paid by the drawees the Long Bills account is debited and the account kept with the paying bank is credited.

### **Drafts Drawn upon Non-Correspondent Banks**

While the bank's extensive branch and foreign correspondent connections enable it to furnish drafts drawn payable in practically any locality, occasionally there comes a call for a draft drawn upon a point where the bank has no connections. In meeting a demand of this kind the draft is drawn upon some bank located in or near the place to which the remittance is to be sent. This drawee bank, however, cannot reimburse itself by charging the account of the New York bank and the latter is therefore obliged to furnish the former with some means of reimbursement before the draft is presented for payment.

This may be done in various ways. If a branch of some foreign bank with which the drawer bank has an account is



located in the city of the payee, the bank draws on that branch for account of its head office. In other instances the bank draws on a bank located in the city of the payee for the account of another foreign bank with which both the drawer and the drawee have accounts. In rare instances the drawer bank reimburses the drawee by sending its sight draft drawn on one of its correspondents located near the drawee bank, or by requesting the drawee to draw at sight in its own favor upon one of the drawer's near-by correspondents or upon the drawer bank itself. In a case of this sort the amount of the draft is credited to an account termed "Funds Retained for Foreign Teller's Drafts," which is charged as drafts drawn for reimbursement are paid.

### Issuance Through Correspondent Banks

Banks throughout the United States are frequently requested by their clients to furnish them with foreign currency drafts. To enable such domestic correspondent banks to fill this demand the New York bank as a banking service extends them the privilege of drawing drafts on any of its branches or foreign correspondents. The foreign banks charge the New York bank and it in turn receives reimbursement from the domestic banks.

To those banks which have made arrangements to use the service is furnished a draft outfit consisting of: (1) a booklet giving the names of its foreign branches and correspondents, (2) draft forms stamped with the name of the domestic bank, and (3) a rate sheet showing the rate of exchange which the correspondent is to charge its clients. As rates change, new sheets are mailed. At times when the exchanges are very unstable this is done every day. The rates quoted for this business are applicable for drawings amounting each to \$1,000, or less. Hence, they are slightly above market rates as is always the case for small lots of foreign exchange. If a larger

draft than \$1,000 is wanted the correspondent is instructed to consult the bank direct for a rate

Certain of the foreign banks charge a tariff for cashing drafts. The domestic correspondent's bill to the purchaser of the draft is therefore the face of the draft in dollars plus the tariff of the foreign bank and its own commission charge. It remits the dollar equivalent of the foreign draft plus the tariff charge to the New York bank in the form of a check or instructions to debit its account. The New York bank makes a small profit out of the foreign exchange transaction, but its most important gain consists in the good-will which is established through extending well-rounded service to its clients.

The draft form supplied to the interior bank has four stubs attached, one of these is retained by the issuing bank, another by the purchaser of the draft, and the remaining two, containing the signature of the officer signing the check, are forwarded to the New York bank together with instructions as to how it is to reimburse itself. From these instructions the bookkeeping tickets and the advices of the issuance of the drafts for the foreign correspondent are prepared. One of the stubs from each draft is also enclosed with the letter of advice. This stub, containing the signature of the officer of the issuing bank who signed the draft, is used by the foreign banker in determining that the draft when presented for payment is genuine.

Each transaction of this sort is recorded in a customers' draft book and when the foreign bank advises that a draft has been paid the entry is stamped out. This book therefore serves as a record of all outstanding drafts. An auxiliary book serves to record the drawings made by each domestic correspondent bank. From these records statistics showing the volume of business transacted for each correspondent are compiled for the use of the traders.

### **Drafts and Transfers Sold by Branches**

Wherever a branch of the bank has an "our" account with a foreign bank the branch draws directly on the foreign bank, where the branch has no account with the foreign bank the branch draws under the protection of the home office. The branch draws for the account of the home office against another branch or a correspondent of the latter bank located in the city of the payee. Both the drawer bank or branch and the home office of the branch drawing the exchange receive advices of the transaction. The home office may handle the reimbursement in a number of ways, but the most common would be to charge the Due from Branches account of the branch drawing the draft and credit the drawee bank or branch.

### **Report to Traders**

A report is prepared daily showing the volume of drafts, letter and cable transfers, and long-time bills drawn on each correspondent and branch, the latter sum expressed in round figures. This report assists the traders of the bank in keeping records of the amounts available for drawing with each of the correspondents with whom accounts are kept and also assists them in computing the amount of cover to be provided. To avoid the possibility of making overdrafts on certain foreign banks while the balances in other banks of the same country remain unused, the traders each week prepare a list of the banks on which drawings are to be made, as has already been mentioned.

### **Payments on Orders of Depositors**

The work of making outgoing transfers sets up a movement of drafts, letter payments, and cable transfers to foreign countries which oblige foreign drawee banks to make payment. Similarly the foreign banks in making transfers to this country

set up a movement of drafts, letter payments, and cable transfers which oblige the New York drawee bank to make payments. Making these payments constitutes the paying work of the foreign teller's department.

### Cashing of Foreign Drafts

In arriving at a decision to make a payment ordered by a foreign customer of the bank, many of the operations applying to cashing a domestic check over the window are performed. The signature is verified by the signature control department, the adequacy of the depositor's balance is determined, and a "hold" for the amount of the payment is placed against the account. Stop-payments are cared for by means of files kept in the department. These may be the ordinary stop-payment orders lodged with the bank by drawers of drafts and transfers, or they may arise from such a situation as when a cable order is substituted by the sender for a letter which is already in the mails.

In making payment under a cable or a letter transfer the method to be followed must likewise be specifically determined; i e., whether by check, by telegram, or by crediting the payee's account, and whether the foreign depositor is to be advised of the payment by mail or by cable. This information may be contained in the instrument which orders the payment, or more usually it will have been sent to the bank in the form of standing instructions.

### Bookkeeping Tickets

After these preliminary measures have been taken the bookkeeping tickets for the transaction are prepared. The debit ticket generally carries a charge to the account of the foreign customer who ordered the payment to be made. At the same time that this ticket is drawn an advice of debit is prepared and sent to the foreign customer. If it is necessary to send

a cable or a telegram in making a payment the cost of this message is accounted for in the usual ways

In case the beneficiary's account is to be credited for the amount of the transfer an advice of credit is prepared concurrently with the credit ticket and sent to the one whose account is credited. Frequently the foreign customer has the bank send a telegram as well as the advice by mail.

Should the bank's instructions be to deliver a cashier's check to the beneficiary, the accessibility of the beneficiary and the acquaintance which the bank has with him determine the course which will be pursued in delivering the check. In case payment is to be made to a well-known party in the city, the check is delivered to him by messenger; if, however, payment is to be made to some payee in the city who is not well known, the bank sends an advice to him requesting that he call and receive his payment upon proper notification. A payment which is to be made to a beneficiary located out of town is forwarded in care of a bank in his vicinity or in care of a representative of the bank. Payments at a distance are frequently made by telegraphic transfer in place of a cashier's check, and if the foreign correspondent sends funds by cable to be paid a beneficiary located out of town the bank always makes the payment by telegraph through its nearest correspondent unless it has specific instructions to make payment by mail. If the foreign correspondent requests the bank to deduct charges the message is sent collect; otherwise the cost of the message is charged to the account of the foreign correspondent. No other charge is made for payments out of town.

In the same operation in which the cashier's check is drawn, receipts are prepared. Three copies are sent to the beneficiary, while the fourth copy is filed in the receipts outstanding file of the department for the purpose of tracing receipts which are not promptly returned. One of the copies sent the bene-

fiary serves the purpose of an advice to him; the other two are signed and returned to the bank. When the signed receipts are returned one copy is retained by the bank while the other is forwarded to the foreign customer. In case it is impossible to locate the beneficiary the bank communicates with the customer who ordered the payment for instructions as to how it shall proceed.

### Payments under Bought Contracts

Payments arising under contracts for purchase cable transfers entered into by the traders are made by the tellers. In case a bought cable is for regular delivery the bank may pay for the exchange immediately, and thus it does by crediting the account of the seller or by issuing a cashier's check. Among the larger dealers of the city it is the custom to pay for cables on the day the transfer is actually effected abroad. This is accomplished by paying for the transfer on the contract date and making a rebate of the interest lost, provided the actual transfer is not effected the same day. On the other hand, it is the custom in dealing with sellers who are not well known to pay for the exchange only after advice is received by cable stating that the transfer has actually been made abroad.

The transaction is handled in much the same manner as an ordinary payment. The instructions come to the foreign teller's department from the traders in the form of a bought contract slip. A distinctive type of contract slip is provided for direct, brokerage, and arbitrage contracts, so that they may be readily distinguished. In making a future bought contract the bank pays the seller at maturity of the agreement. The traders hold the contract slip until the time of payment arrives, then they forward it to the foreign tellers who handle it just as they would a spot contract.

The purchase of foreign exchange in New York is really the purchase of a portion of a foreign bank balance. The

foreign bank holding the balance debits the seller of the exchange and either credits the purchaser's account or makes a remittance to a second foreign bank according to the orders of the purchase. The seller cables the foreign bank to make the transfer. In addition the purchaser sends a letter or cable instructing the foreign bank to receive the deposit and either to hold the amount or to dispose of it in the manner desired.

### **Purchase and Sale of Foreign Money**

It is not the policy of the bank upon the practices of which this is written to deal actively in foreign money, but as a service to customers it undertakes to purchase their requirements and make sales to them. Transactions of this sort are made with foreign money brokers of the city.

## CHAPTER XVIII

### TRADING IN FOREIGN EXCHANGE

#### The Foreign Exchange Market

In preceding chapters the various types of foreign exchange transactions passing through the bank have been described. The plan has been to discuss each of these transactions alongside the better understood domestic transaction which it most resembles. In addition to these transactions there are others connected with international banking which have no direct parallel in the domestic field. These consist of purchases and sales of foreign exchange in the open market. This market comprises the dozen or more large banks and other dealers in foreign exchange in New York City, and also includes banks doing a foreign exchange business in other cities of the United States and in all parts of the world. Large international business houses having deposits in various centers abroad also constitute a part of this market. Open-market operations are always in large amounts and are consummated generally by cable, telegraph, or telephone. In New York City, brokers play an important part as intermediaries between the dealers in foreign exchange and some of them enter engagements on their own initiative.

The bank is represented in this open market by the foreign exchange traders. In addition the traders have the function of quoting rates for the use of other departments of the bank and for the information of clients, especially other banks.

It would be futile to attempt to explain trading in foreign exchange within a single chapter of a book of this sort. Such trading is a profession requiring years of experience for the attainment of skill. It would be equally out of place here



to discuss the theory of foreign exchange concerning which volumes have already been written on the subject. Hence, in succeeding pages only some of the general features of foreign exchange trading and related activities will be discussed.

### **The Work of the Foreign Traders' Department**

The work of the foreign traders' department divides itself along three distinct lines

1. The actual operations of purchasing and selling exchange, quoting rates, etc., performed by the traders themselves
- 2 Keeping the position sheets
- 3 Keeping the "due from foreign banks" ledgers

#### **1. Trading Operations—Nature of Foreign Exchange Business**

Dealing in foreign exchange consists in essence in trading in foreign bank balances. Purchases of foreign exchange consist merely in purchasing items drawn in foreign currency and payable abroad. These items are remitted to foreign banks where they are collected or discounted and credited to the account of the sending bank. Balances built up in this way constitute the sending bank's supply of exchange, and they are built up largely from commercial bills purchased from or collected for customers. In the open market, bankers' bills, including cable transfers, may also be bought. Sales of exchange consist of sales of bankers' bills (cables, letter payments, drafts, foreign currency import credits, etc.) against the balances built up in this way.

#### **Foreign Exchange Rates**

The price of foreign exchange is expressed in terms of the amount which a single monetary unit of a foreign country will command in terms of local currency. Thus a quotation

of 19 cents for franc exchange means that the bank or broker making the quotation is willing to buy or sell, as the case may be, bills drawn in francs and payable in France at the rate of 19 cents per franc

Rates of exchange usually refer to prices of bills of exchange. Such rates are termed "commercial parities." Contrasted with commercial parities are mint parities, which refer to the ratio of the bullion content of a unit of the standard money of a foreign country to the bullion content of the local monetary unit, alloy being disregarded.

Thus the British pound sterling contains 113.002 grains of pure gold and the United States dollar has 23.22 grains. For example, to find the mint parity of sterling exchange it is necessary merely to solve the following proportion.

$$\begin{aligned} 23.22 \quad 113.002 &= 1 \quad \text{\textit{x}} \\ \text{\textit{x}} &= \frac{113.002}{23.22} = \$4.8665 \end{aligned}$$

It is apparent that the mint parities of exchange are fixed rates since the metallic contents of the monetary units of the various countries are fixed. The commercial parities, on the other hand, fluctuate with demand for and supply of bills of exchange. The foreign exchange dealer is not particularly concerned with mint parities except in connection with gold shipments which will be described presently. The main interest is in the commercial parities.

### Factors Influencing Movements of Exchange Rates

Movements in foreign exchange rates are due both to broad underlying factors and to momentary conditions. In trading both have to be taken into consideration. The broad factors influencing movements in exchange rates are:

- 1 Exports and imports of merchandise.
- 2 Remittances for freight, insurance, etc

3. Remittances for expenses of tourists and travelers
4. Remittances made by immigrants to their home countries
5. International loans
6. Payments for interest and dividends on foreign investments
7. Gold movements

As between any two countries, undoubtedly the most important factor influencing the foreign exchange market is the movement of merchandise. Exports bring into the local market a supply of bills drawn upon buyers in the country to which the shipment is being made. They increase the supply of exchange and therefore tend to depress the market. Imports, on the other hand, create a demand for bankers' bills to be remitted abroad in settlement and they tend to raise the market. If, therefore, a country passes through a period of unfavorable trade balance, i.e., if for considerable time its imports exceed its exports, exchange on other countries will be high in its market, while if it has a favorable trade balance foreign exchange will be low. Between two countries merchandise shipments tend to depress the exchange of the buying country and to elevate that of the selling country.

The foregoing statement, however, needs modification. There are other factors than foreign trade operating to influence the foreign exchange market. First should be mentioned payments for freight, insurance, and other services. If a country is a large owner of ships and has insurance companies doing an extensive overseas business the effect on the exchange market is just the same as though the amount earned from these enterprises was added to that country's exports. The same is true of foreign investments. Those countries in which there is a large holding of foreign securities reap a reward in the form of interest and dividends, and these remittances tend to bolster the prices of the exchange of these countries.

in foreign markets just as do exports. Likewise, remittances of immigrants to the home country and expenses of travelers visiting a country tend to bolster up its exchange rates in foreign markets.

International loans may also influence exchange rates. The effect of interest and dividend payments on the exchange market have already been mentioned. Likewise, when a long-term loan is to be placed in a foreign market or is to be paid off, the necessity of moving the funds from one country to another, if it arises, will influence exchange rates tending to depress the exchange of the remitter and to increase rates on the exchange of the country receiving the funds.

Short-term bankers' loans from one country to another are frequently employed. In a free market, capital flows quite readily to the center which will pay most for the use of it. If on a certain day bankers in Paris, for example, find that the interest rate for short-time loans in New York is 6 per cent while the rate in Paris is only 5 per cent they immediately send funds to be loaned in New York. Transactions of this sort are handled most commonly by having the American house which is to place the loan draw bills of exchange upon the foreign bank which desires to lend the money, sell these foreign bills in the New York market, and use the proceeds for the purpose of the loan. When the initiative in these operations is with the foreign bank, the bills are called "foreign loan bills." When a local bank initiates such a transaction and borrows funds abroad, the bills are termed "finance bills." This is merely a technical difference, however, and is not discernible from the face of the bill. From the standpoint of the trader both have the same effect in temporarily increasing the supply of exchange.

These international loans are for short terms, usually 90 days, and at the end of this time the borrowing bank is obliged to go into the market to buy bills on the foreign point with

which to repay the foreign bank for the loan. These loan and finance operations therefore create only a temporary supply of exchange in the borrower's market which later changes into a demand for foreign bills.

### Gold Shipments

Normally, foreign exchange transactions consist of trafficking in bills of exchange of various kinds and no actual currency need be used. The bank builds up foreign balances largely by purchasing commercial bills drawn in foreign currencies, and it sells exchange in the form of checks, cable transfers, and other forms of drafts drawn against these balances. At times, however, it may be more profitable to build up foreign balances by exporting gold coin or bullion to foreign banks. Conversely, foreign banks may find it more profitable to build up dollar balances in America by sending metal rather than bills of exchange.

When gold may be freely had and shipped from one country to another without restriction, the exchange rates can never fluctuate very far as a result of inequalities in the supply and demand for bills. Equilibrium will be restored by shipments of gold. For example, if during the early summer months an American bank should find that its stock of pounds sterling abroad is running low owing to the demands made upon it by American importers of English cloth, hardware, etc., it may find that the cost will be, say, \$4 91 for each pound sterling needed to replenish its balance. The cotton and grain bills have not yet come into the market and sterling is scarce, hence it will have to bid the market up. Rather than pay \$4 91 for sterling bills it is to the bank's interest to restock itself instead. Either gold bars or United States gold coin, preferably the former, is used for making the shipment. The English bank receiving the shipment has the gold assayed and weighed and credits the shipper for the equivalent in

pounds sterling In this way, the American bank can buy the metallic equivalent of an English pound sterling for \$4 8665, the mint par decreed by law If it costs 3 cents per pound sterling to ship the gold—which cost is made up of packing charges, cartage, freight, insurance, assaying charges abroad, and interest from the time the gold was purchased to the time that the banker abroad gave credit for the shipment—the net cost to the bank of restocking itself will be, roughly, \$4 90 per pound sterling, or 1 cent cheaper than if it had bought the bills offered in the market at \$4 91 From the American standpoint the price of exchange at which it becomes more profitable to ship gold than to buy bills of exchange is termed the “gold export point”

If conditions were just the opposite and sterling depreciates, say, to \$4 83, British bankers would find that their balances in dollars in this country would be costing them too much; that is, for every pound sterling expended in the market they would be increasing their balances by only \$4 83 instead of around \$4 86, as is normally the case They would therefore buy gold in England, getting \$4 8665 worth for each pound sterling, and ship the gold Their costs would be about 3 cents per pound sterling and therefore they would never allow sterling to fall very far below \$4 8665—03, or \$4 8365, if they are able to procure the gold From the American viewpoint this is the gold import point and it marks the minimum price to which sterling exchange may fall, provided there is a free movement

### Foreign Exchange Rates and Gold Shipment Point

Normally, foreign exchange rates fluctuate within the gold export and import points Shipments of gold, however, are so closely related to bank reserves, rates of interest, prices, etc., that it is a settled policy with the central banking institutions of almost every nation to control such movements

Furthermore, the various governments in time of economic stress, such as war, quite readily prohibit gold movements. Therefore, while in the chief countries of the world it is the boast that gold may be freely had for export or may be freely imported and changed into coin, in practice the matter does not work out that way. When the foreign exchange dealer most wants to obtain gold for shipment he finds it is not to be had. There are, then, certain influences which are strong enough to carry exchange rates beyond gold shipment points.

As an example, the condition prevailing in the market for Spanish exchange in New York at the close of the Great War may be given. The mint parity of the Spanish peseta is 19 3 cents in terms of United States money. The gold export point of the peseta would therefore be about 19.65 cents. After the armistice Spanish exchange was quoted in New York at above 20 cents per peseta. As would be expected, a shipment of gold from New York to Madrid was made. Although only a small amount was shipped the price immediately fell to a point substantially below the export point.

Sometime afterwards a change in the elements affecting the exchange market depressed the price of pesetas to below 17 cents. The gold import point is about 18 75 cents. The Bank of Spain, however, refused to release gold for export. As a result the price of pesetas in New York remained substantially below the import point.

A knowledge of these broad economic facts does not enable one to trade in foreign exchange, else foreign exchange traders would be more plentiful. The ability to trade consists largely in being able to sense the monetary trend of the market and take advantages of these tendencies.

### Receiving Quotations from Abroad

Owing to the fact that communication between the various exchange markets and the transfer of funds from one to

another is so readily effected by means of the cable, the open market in foreign exchange is world-wide. The rate at which exchange can be bought or sold in New York, for example, depends largely upon the rates prevailing in such financial centers as London, Paris, Berlin, etc. London, however, is the foreign exchange center of the world and the traders as the first part of their day's work study particularly the latest developments in that market.

The business day in Europe commences about 5 hours before the American day, so that trading is in full swing before the market here has opened up. The traders of the American bank are therefore in the fortunate position of being able to see a large part of the market in operation before they actually do any trading. This information is gleaned from quotations and market reports sent by cable from certain of the bank's correspondents and certain other dealers with which it trades. For the ready reference of the traders a parity sheet is prepared from the quotations coming from the foreign markets.

### The Parity Sheet

The parity sheet consists of a tabulation of the rates of the chief foreign exchange markets of the world expressed in the nomenclature of the American market. Space is provided on the parity sheet for entering the quotations of London, Paris, Belgium, Italy, Holland, and Berlin, in detail, while those of other markets are shown in more condensed form. For any one of the chief foreign exchange centers the parity sheet shows the cable rate and the items which must be added to obtain the demand rate, and the rates for 30-, 60-, and 90-day commercial drafts. The parity sheet also shows the discount rates for commercial paper prevailing in each foreign market.

Foreign rates are received by cable at different times as



the day's trading progresses. As the changes come in, corresponding entries are made on the parity sheet. The parity sheet thus at any time of the day furnishes the traders with a composite picture of the foreign exchange market of the world and its tendencies.

### Quotation of Foreign Exchange Rates

In this connection it may be well to describe the method of computing the commercial parities and the system used in quoting foreign exchange rates in the United States. The foreign financial centers quote the exchanges in terms of their own currencies. For example, London cables quote so many francs, lire, etc., to the pound sterling. The traders in New York are interested in the value of these exchanges in terms of the dollar, and they have the dollar equivalents, or so-called market parities, computed as a basis for entry on the parity sheet. If sterling was worth \$4.85 in New York at the close of the day before and the London cables state that 1 pound sterling will buy 25 francs, the traders simply divide 25 by \$4.85, which gives 5.155, the number of francs which a dollar will buy. This rate is entered in the space for French exchange on the parity sheet. Similar computations are made for Belgian and Swiss francs and for lire, for these currencies are quoted in the United States as so many francs or lire to the dollar.<sup>1</sup>

The pound sterling, mark, peseta, krone, and others, however, are quoted as so many cents to the foreign monetary unit, which is quite a different matter. Thus the sterling rate is expressed at \$4.86 to the pound, the mark at 23 cents, the peseta at 19 cents, etc. To arrive at these figures the opposite viewpoint is adopted. Instead of computing the number of

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<sup>1</sup> At the time of writing a movement that had been started by prominent bankers to quote franc and lire exchange in terms of cents has been brought to a successful issue. All quotations made in New York City are now in terms of dollars and cents per unit of foreign currency.

foreign units which a dollar will buy, the number of cents which the mark, peseta, etc., will purchase is computed. Thus, if the London rate states that 20 marks will buy 1 pound, and therefore \$4 85, 1 mark will be worth one-twentieth of \$4 85, or 2425 cents.

When francs or lire are low, it takes more of them to make a dollar and the rate is a larger number. When sterling, marks, kroner, etc., are low, they are worth fewer cents and the figure is a smaller one. This difference in the method of quoting the rates is often confusing to the layman.

### Classes of Quotations

Each quotation is divided into several classes according to the types of bills involved. The most common classes are as follows: cables, demand or checks, 30-day bills, 60-day bills, and 90-day bills. The cable rate refers to the price of a cable transfer and it expresses most nearly the exact market relation between two currencies. It is, of course, the highest rate because a bank selling such a transfer does not have the use of the funds involved for any appreciable length of time. Its account abroad is charged with the amount of the transfer within a few hours after it receives the selling price from the customer. Viewed from another standpoint the higher rate for cable transfers represents the price which the purchaser must pay for the privilege of using his funds right up to the moment that his payment falls due abroad, and taking advantage of any intervening fluctuations in the rates of exchange.

The quotation on demand exchange, or checks, refers to the price of items drawn payable at sight or on demand. The rate for 30, 60, or 90 days' exchange refers to the price of bills drawn payable 30, 60, or 90 days after date or sight. Each of these rates will necessarily be lower than the rate for cables in proportion to the additional time involved.

In addition to the trend of the exchange markets abroad, which finds expression in the parity sheet, the local market is also studied for the latest developments here before any policy for the day is decided upon. This is done by interviewing the brokers who come in during the early part of the morning with offers to buy and sell.

### Quoting Rates

The policy of the bank having been decided upon, the traders are ready to quote the rates at which they will deal in exchange. These rates are of two classes: the buying rate, or that which the bank offers to pay for exchange, and the selling rate, or that at which it will make sales. New York City customers receive these rates by calling over the telephone, by sending their brokers, or by calling in person. Telephone calls are of such great volume that a force of telephone clerks is required to answer them. The domestic clients of the bank, composed of banks and large exporters throughout the country, receive the quotations by telegraph, and the foreign customers in various parts of the world receive them by cable. Many of these customers have standing instructions with the bank requesting that the rates on certain currencies be sent them at stated times. These instructions are kept on a set of rate cards, one card for each client. The rates are sent forward by writing them upon the cards which are sent to the telegraph and cable department from which messages are despatched.

Rates quoted to the above classes of customers constitute what are termed "service rates." They are intended merely to give information regarding the state of the market to such customers as request the bank to do so. The bank sends these quotations without charge, as a banking service. Distinct from service rates are firm rates. These are actual offers on the part of the bank to buy or sell at the rate quoted. Firm rates are quoted only on special application.

### Handling Orders to Buy and Sell Exchange

These quotations which the traders have distributed among the customers of the bank soon begin to bring results in the form of orders to purchase or sell exchange. In addition, the wires are kept busy with offers to purchase or sell, coming in from out-of-town dealers and from local brokers. Many of the latter visit the traders' department in person to submit bids and offers. Out of this great mass of orders, bids, and offers the traders make their contracts.

The term "contract" as used in the parlance of the foreign exchange market must not be construed to mean a formal document signed by both contracting parties. At best the agreement will generally take no more formal shape than that of telegrams or cables passing between the two parties—one message constituting the offer and the other the acceptance. Engagements are most frequently entered into orally to be confirmed immediately in writing. For that reason the integrity of the individual dealers many times constitutes the only protection of the bank. Contracts are entered into, therefore, only with such parties as have had previous dealings with the bank or as have come properly introduced.

### Purchase and Sale Book

When a transaction has been completed the details are entered upon the contract slip with which the reader has already become familiar in the work of the foreign tellers. The trader who made the transaction initials this slip and entry is then made in a purchase and sale book. This book has a section for each foreign currency, the bought contracts being entered on the left-hand page and the sold contracts on the right-hand page. It is consulted from time to time during the day for the purpose of determining the volume of business transacted and in connection with the position sheet, to ascertain the state of the foreign balance. Each entry shows the

name of the contracting party, the kind of contract—whether it be demand or future—the amount, and the rate. Each line and therefore each entry in the book has a number. This number is stamped upon the contract slip in order that it may readily be traced in case of need. After a convenient number of transactions have accumulated they are delivered to the foreign teller's department or to the foreign discount department against receipt, where they are executed in the manner already described in the previous chapter.

### Spot and Future Contracts

Foreign exchange contracts are made either for spot or for future delivery. A future contract differs from a spot contract only in that delivery and payment for the sum involved is to take place at a stated future time. Within the traders' department future contracts are handled in every respect like spot contracts, being entered upon the same contract slips and recorded side by side in the same book. In ascertaining the total amount bought or sold, both spots and futures are added together and regarded as one lump sum. While spot contracts are sent to the foreign tellers to be executed immediately, future contracts are confirmed, filed away, and sent to the tellers on the day of maturity.

The future contract in foreign exchange is a very useful device for exporters and importers who have a constant use for quantities of foreign exchange. The manner in which merchants employ these future contracts and the way in which the bank handles them can best be illustrated by an example. A clothing manufacturer imports £10,000 worth of wool every month from Australia. To enable him to carry on his business on a fixed basis for the ensuing year, that is, to compute his costs, his selling price, and his profits in advance, he must know what the sterling exchange with which he is to pay for his raw material will cost him. Accordingly he

contracts with his bank to buy the necessary £10,000 each month for 12 months. Suppose that the state of the exchange market is such that the bank expects higher rates in the future. It quotes the importer a certain rate for his January instalment, a slightly higher rate for his February requirements, a still higher rate for the £10,000 to be sold him in March, and so forth on a sliding scale for the whole year. Thus the importer is able to know in advance just what each monthly shipment for the ensuing year will cost him.

In dealing in futures the bank does not act as a speculator in exchange. It covers each sale by an immediate purchase of a like amount of exchange and vice versa, hence it does not enter into a contract for future delivery unless it knows in advance that it can buy cover immediately. Cover is not generally procurable for a longer period than one year; therefore future contracts for a longer period are seldom met with, in fact the majority of futures are for a period of 6 months or less.

The purchase of cover for a future sold contract takes the form of a purchase of exchange for future delivery to the bank. Such a purchase of a future serves the same economic function as the sale of a future. Let it be supposed that an American exporter has contracted to ship foodstuffs to Great Britain amounting to £10,000 each month. The exporter is interested in knowing what price he will be able to obtain for the sterling bills which he draws upon his customer in order that he may intelligently fix his selling price. Accordingly he enters into an agreement with his bank whereby the latter agrees to purchase his bills at a certain price for each month's delivery.

Thus as the given instalment of the future sold contract matures, the bank meets its obligations to furnish sterling to the purchaser by means of the sterling brought in by the maturing instalment of the future bought contract. The bank's

profit from the transaction consists in the difference between its sold rate and its bought rate, and since both contracts are entered into practically at the same time, based on the existing rate of exchange, the bank's profit is in no wise affected by subsequent fluctuations in the exchange rates

### Arbitrage Transactions

Since the bank buys and sells in all the markets of the world and since it has information as to the rates at which exchange can be bought and sold in all these markets, it is frequently enabled to purchase exchange in one foreign market for sale in another at a profit, and it is also frequently able to purchase its requirements in one kind of foreign currency through an intermediate market rather than direct. Operations of this sort are termed "arbitrage" transactions.

Arbitrage transactions in foreign exchange can best be explained by the use of an illustrative example. Let it be supposed that on a given day marks can be sold in the New York market for 23 5 cents. At the same time the New York dealer can purchase sterling at the rate of \$4 85 per pound and he can buy marks in London at the rate of 20 8 marks per pound sterling. Should a bank in New York desire to accumulate a stock of marks by direct dealing, it is apparent that the cost would be 23 5 cents per mark, i e., the New York rate. The bank can, however, buy 1 pound sterling for \$4 85, and with each pound sterling it can purchase in London 20 8 marks. Since 20 8 marks can be purchased for \$4 85, in this way, the cost of 1 mark will be \$4 85 divided by 20 8, or 23 3 cents. By purchasing its stock of German exchange in this roundabout way the New York bank can reap a profit of 2 cents per mark, i e., the difference between the direct rate 23 5 cents and the arbitrage rate of 23 3 cents. If the transaction involves a large quantity of exchange, as is usually the case, this margin results in a handsome profit for the bank,

In practice the arbitrage transaction takes a variety of forms. Instead of three markets being involved, there may be a larger number. Any foreign currencies may be involved although the pound sterling is almost always used as one of them, since this currency enjoys such a wide market. The essence of the arbitrage transaction is, however, the same in all cases. It consists in buying a commodity, i.e., foreign exchange, wherever it can be bought cheapest and disposing of it wherever the best price can be obtained.

From the standpoint of the foreign exchange market as a whole the possibility of engaging in arbitrage transactions acts as a constant force toward the equalization of exchange rates in all markets. As soon as rates show signs of sagging in one market foreign exchange dealers from all outside points flood this market with orders, and as a result of the increased demand the rates advance. Likewise in a market which shows signs of advancing, traders from outside markets make excessive offerings of exchange through their arbitrage transactions until the increased supply forces the rates down to the common level.

## 2. Keeping the Positions

In order to carry on their operations to the best advantage the traders must know positively and quickly not only where the bank has funds available abroad and the amounts as of the given day, but also what the status of the balance will be on future dates as a result of deposits and withdrawals which are in transit on the mail steamers, and as a result of the future contracts which have been entered into. The due from foreign banks ledgers, which contain the foreign currency balances, do not give this detailed description. These are merely memorandum accounts used for checking the entries made to the actual accounts kept by the foreign banks. They leave out of account entirely the future contracts which



have not yet matured. Entries in these books are made as of the date that the transactions are consummated here, not as of the date when the entries are actually passed to the accounts abroad. Moreover these ledgers are always a day behind time, for they are built up from debit and credit tickets drawn in the various departments the preceding day. To fill the need for information of this sort two "position sheets"—the sight position and the cable position—are kept.

### The Sight Position

The object of the sight position is to show the amount of foreign currency available for drawing by means of sight drafts and those of longer maturity. The sight position lumps all the due from foreign banks accounts in a particular country together and simply lists the total stock of each currency on hand at the beginning of the day, the purchases and sales of exchange made during the day, and the new balance resulting in each currency. Credit balances are shown in black ink, while debit balances representing overdrafts are entered in red ink. Not including the cable transactions, the purchases are composed of bills of exchange which have been purchased and the sales consist of foreign drafts which have been sold. These bills and drafts go abroad on the same mail steamer, and therefore the sight position shows the status of the balances abroad which would result if this last steamer arrived safely abroad and if no further purchases or sales of exchange were made in the meantime. This position is accordingly a sort of gross inventory of the stock of foreign exchange classified by currencies.

### The Cable Position

The object of the cable position sheet (Form 80) is to show the balances available abroad for drawings by cable, together with the changes in these balances, which will result

as items in transit reach their destination This position is kept in detail according to foreign banks with which deposits

April 1921																
		1	2	4	5	6	7	8	9	11	12	13	14	15	16	
Banca Commerciale Italiana London		26.1	7.50	\$20	\$20	\$20					\$10			\$10		
Foreigne Loan Trust Co Paris		13,000	13,700	13,150	\$100	\$100			\$100					\$100		
Bank National de Grece Athens		7.0	10.00			1.00			1.00					1.00		
Bank Handelskredit Berlin Zurich		7.0							4.0					1.00		
I P S Yokohama		12.0														
De Nederlandsche Bank Amsterdam		17							\$10					1.00		

Form 80 Cable Position Sheet (Size  $27\frac{3}{4} \times 18\frac{1}{2}$ )

are maintained On a given date in the designated column opposite each bank's name appears that day's balance available for cable transfers, in the following column appears the net

debit or credit changes which will occur in the balance on the following day. These changes are computed in the following manner: to the deposits in transit due to arrive on that day are added the bought cable transfers value date as of that same day. This gives the total credits in prospect for that account for the given day. The total prospective debits for any day are obtained by adding to the draft advices and other debits in transit due to arrive on that day all cable transfers sold with value date as of the same day and the amounts required to meet maturing drafts drawn under the bank's import commercial credits and accepted by the given foreign correspondent. The difference between the total debits and the total credits gives the net change to be expected on the given day. This amount appears in the proper date space in red ink if a net debit, and in black ink if a net credit.

In a similar way each of the succeeding columns to the right contains the net change to be expected in the foreign account on each future date up to 15 days. Today's column therefore always shows the balance of the account as it appears upon the correspondent's books, so far as the bank is able to determine it. Succeeding columns show the accretions to or deductions from this balance which will result from transactions already entered into by the bank. To determine the prospective balance of a future date it is necessary merely to add today's balance to the net change in prospect for the intervening period of time.

#### **The Classification of the Balances According to Maturity Dates**

The entries upon the position sheet and the classification of the foreign balances according to maturity dates is accomplished in the following manner: Disregarding cable transactions for a moment, all letters applying to purchases and sales of exchange made on a certain day are sent abroad on the

same mail steamer. From the outgoing mail department the exact date when that steamer will arrive abroad is ascertained. From these data a set of steamer sheets each of which is labeled at the top with the name of the steamer and the day on which it will arrive abroad is prepared. Each of these sheets contains a number of sections representing miniature due from banks accounts. The material for postings to these accounts comes in the shape of reports from the various foreign departments, showing the purchases and sales of exchange classified by the foreign accounts to which they apply. These figures are transposed to the steamer sheets, each entry to its particular account, and the net change, whether debit or credit, resulting in each account from the material carried on this steamer is ascertained.

These balances are posted in round numbers by thousands in a position book. This book may be described as a ledger containing the position account with each foreign correspondent of the bank. In this book the accounts are divided sectionally by days. In posting from the steamer sheets the entries are transferred to the debit or credit side of the particular correspondent's account and this entry is placed in the date section corresponding to the day when mail from the particular steamer is expected to reach the correspondent. Cable transfers, both bought and sold, are posted directly to the position book as of the value date specified in the cable. Amounts required to meet payments against the bank's commercial credits are also posted to this book. This book therefore shows each foreign balance divided into sub-balances according to the dates on which the component parts of the balance become available by cable.

These sub-balances are then posted to the cable position sheet, each in the corresponding date column and opposite the name of the proper bank. The sub-balances derived in the same manner on the following day are entered in the space

just above, a single sheet sufficing for one week and the latest balances appearing at the top.

### **Documents Payment Accounts**

Bills of exchange which are to be paid before the accompanying shipping documents are surrendered have no determinable maturity date so far as the bank is concerned, inasmuch as the consignee is usually given a certain length of time in which to make payment. Usually he is given 30, 60, or 90 days in which to pay his draft, and payment before the stipulated time is rewarded by a rebate of interest. The bank has no way of knowing when these payments are made abroad, hence record of such remittances is made in a special Documents Payment account which appears on the steamer sheets, in the position book, and on the cable position sheet merely as a potential balance. From time to time the foreign banks holding such bills cable the amounts which have been taken up and credited to the bank's account. Upon the receipt of these cables these credits are posted to the proper date column in the regular manner.

### **Bills Held in Portfolio**

As a general rule all foreign bills of exchange purchased by the bank are sent abroad with the instructions that they be discounted and placed to the credit of the bank's account immediately. At times, however, when the discount rates abroad are unfavorable and change for the better is anticipated, a portion of the bills—generally the long-term ones—are sent with instructions to the foreign correspondent to hold them in portfolio. Then when the discount rates abroad become favorable, the bank cables that the bills be discounted, thus obtaining a greater net balance than if the bills had been discounted immediately. These portfolio accounts are also shown separately on the position sheets.

Many foreign banks keep bills in foreign portfolio, more particularly as reserves to be thrown upon the market when the exchange rates of their currency become unfavorable. By this means they prevent their rates from dropping below the gold export point and thereby conserve their gold reserves. In the United States, however, gold movements are regulated by the federal reserve banks, theoretically at least, by raising or lowering the discount rate as the case may require and no significance attaches itself to the portfolio accounts of the American bank, save that mentioned in the preceding paragraph.

### Use of the Positions

Both the sight and the cable positions are completed at the close of each day and are handed to the traders in the morning who guide their policies accordingly, replenishing the balances that are running low at the expense of those which are becoming excessive.

This work of replenishing is done either by ordering the foreign correspondents holding excessive balances to make cable transfers to those with whom the balances are too low, or by directing the remittances of the next few days chiefly toward the low balances and making the sales of exchange out of the greater balances. The latter plan is carried out by making the necessary apportionments on the lists which are sent to the foreign discount department, the foreign collection export department, and to the foreign tellers. The foreign discount department receives each week a list of the banks to which they are to send the bills which have come into their work and the foreign tellers likewise receive a list of the banks against which they are to draw their drafts, letter payments, and cables. By means of these lists expensive overdrafts in certain accounts and idle balances in others are avoided.

### **The Future Book**

To show details regarding future contracts outstanding a future book is kept by the department. This book, which is divided into sections according to currencies, lists all future bought and sold contracts according to the months in which they expire. The pages are ruled to contain information showing the name of the party who bought or sold the future, the month in which delivery is to be made, the foreign currency amount, the rate, the tenor, the dollar amount, and it contains a separate section at the right of the page for withdrawals showing when the withdrawals are made, the foreign currency amount, and the dollar equivalent.

### **3. Due from Foreign Banks Accounts**

The position sheets show the approximate balances of the more important due from foreign banks accounts expressed in round numbers by thousands and quickly compiled from special reports sent to the traders by various foreign departments. The due from foreign banks accounts ledgers contain detailed entries made from debit and credit tickets arising in the various departments, and they therefore show exact balances.

The books for this section of the accounting work of the bank consist of the due from foreign banks account ledgers proper, the control ledger for these accounts, and a statement book. These books are divided into sections by foreign currencies. All tickets applying to these records are sent at the end of each day by the various departments in which they originate to the ticket journal department, the workings of which will be explained in subsequent chapters. This department then sends them on the following morning to the due from foreign banks control ledger where they are sorted according to banks and the dollar amounts posted in total. Entries in this book are made in dollars for the reason that

a report of the status of these accounts is sent daily to the general bookkeepers of the bank who are interested only in dollar amounts. The balances are recorded in the statement book in round numbers by thousands for reference by the traders of the bank. From the control ledger the tickets pass to the ledgers proper to be entered in detail. Here the date of the entry, the steamer date, a brief description of the item, the rate, the tenor, terms, number of the item, due date, value date, foreign money (net amount), foreign money (face amount), and the amount in dollars are entered.

Every entry posted relates to a foreign currency item and the bookkeeping tickets give the amount in foreign currency, the rate, and the dollar equivalent. Both the foreign currency and the dollar amounts are posted in the ledger. When a proof is made, therefore, two balances are to be checked. The amounts in foreign currency are compared in a rough way with the balances shown on the position sheets. The amounts in dollars are compared with the control ledger for the due from foreign banks accounts.

So far as possible all entries are checked against the original material from which the tickets originated, remittances sent forward by the foreign discount department are checked against the office copies of the remittance letters, cable transfers are checked against the cable copies, sales of foreign drafts and letter payments against the draft and letter payment stubs, etc. When the advice letters are received from abroad stating that the accounts have been debited or credited as of certain dates for certain amounts, these advices are likewise carefully compared with the entries on the books. Occasionally this comparison brings out differences between records of the bank and its correspondents. In such cases adjustments are made. For example, in case a remittance is purchased with a certain value date and the bank abroad gives credit as of a later date, the party from whom the



purchase was made is requested to make good the difference in interest

The balances of these accounts are compared with the positions twice a month and are reconciled regularly by the reconciliation department with the balances reported from abroad. Every six months the stocks of foreign currency represented by the balances on the due from foreign banks ledgers are appraised at the prevailing market rate. The inventory figures so derived are compared with those of the previous half-year and show the profit or loss from trading during that period.

## CHAPTER XIX

### THE BANK AS TRUSTEE, EXECUTOR, AND CUSTODIAN

#### Trust Functions

The operations described in the foregoing chapters are commercial banking functions. Prior to the enactment of the Federal Reserve Act, national banks were authorized by law to exercise only commercial banking functions. An amendment to that act approved September 26, 1918, permitted any national bank to apply for and receive permission from the Federal Reserve Board to engage upon all the trust functions exercised by state banks and trust companies in the state in which the particular bank is located, provided the exercise of such powers is not restricted by local statute. Since this amendment, national banks in constantly increasing numbers have taken advantage of the opportunity afforded them.

Some of the trust functions which may be performed are the following:

#### 1. For individuals:

Executor under a will

Trustee under a will or deed

Administrator of an estate

Guardian of the property of a minor.

Committee of the property of incompetents.

Custodian of securities and other property

Care of investments in real or personal property

#### 2. For corporations:

Trustee for bondholders under mortgage indentures

Trustee under other corporate agreements

Depository under escrow agreements, voting trusteeships, reorganizations or adjustment agreements, subscriptions to stocks or bonds, and of claims against bankrupts.

Transfer agent

Registrar of securities

Fiscal agent, paying dividends, coupons, and principal of bonds and notes

### **Fitness to Act in Fiduciary Capacity**

Little need be said in support of the pre-eminent fitness of a national bank to act in a fiduciary capacity. The advantages are obvious. The bank has practically perpetual existence and may engage in undertakings requiring an indefinite period of time for consummation with the assurance that it will be in a position to complete its task. It has a regular place of business, its hours are fixed, it does not take vacations, and it is unlikely to abscond or speculate with funds or render false accounts. A bank's business is handling financial matters, and from practice it becomes expert in all the complex details connected with trust affairs. Its business is of sufficient volume to permit it to employ specialists for each section of the financial field which it covers.

The principal business of the trust department of a bank is to attend to the fiduciary matters entrusted to its care, it is never too busy with other affairs, as is so often the case with individuals, to give the proper attention to business placed under its charge. Fiduciary matters are held by the bank sacred and confidential.

The safety of a bank is a consideration of prime importance. The trust department of a national bank is hedged about in its activities by state and national law and in addition its affairs are subject to rigid examination by both state and national examiners. In New York, as in most states, a bank

having trust powers is required to deposit securities representing 10 per cent of its capital with the state banking department to guarantee the faithful performance of its duties. Perhaps the most important guarantee of all, however, is the reputation of the bank. Behind all these legal requirements and behind the capital and surplus of the bank stands its most important asset—the good name which it has carefully built up through years of fair and honorable dealings.

### Organization of Trust Department

As has already been indicated national banks derive their authority to operate trust departments from the Federal Reserve Act which gives the Federal Reserve Board power "to grant by special permit to national banks applying therefor, when not in contravention of state or local law, the right to act as trustee, executor, administrator, registrar of stocks and bonds, guardian of estates, assignee, receiver, committee of estates of lunatics, or in any other fiduciary capacity in which state banks, trust companies, or other corporations which come into competition with national banks are permitted to act under the laws of the state in which the national bank is located"

It is further provided that "in passing upon applications for permission to exercise the powers enumerated in this subsection, the Federal Board may take into consideration the amount of capital and surplus of the applying bank, whether or not such capital and surplus is sufficient under the circumstances of the case, the needs of the community to be served, and any other facts and circumstances that seem to it proper, and may grant or refuse the application accordingly, provided, that no permit shall be issued to any national banking association having a capital and surplus less than the capital and surplus required by state law of state banks, trust companies, and corporations exercising such powers."

Preliminary to the opening of a trust department and

following the granting of permission to do so, it is necessary for a national bank to establish by resolution of its board of directors a separate department of the bank under officers whose duties are prescribed by the directors. The directors are required to designate two or more officers or employees to have charge of trust securities. These employees are required to furnish bond for the faithful performance of their duties.

When the trust department is opened its books and records are required to be kept separately from those of the bank proper and a separate account is established in which trust funds in cash are deposited. If such funds are treated as a general deposit of the bank, the bank must secure them with a deposit of United States bonds or other approved securities lodged with the trust department. Securities and all assets other than cash held in a fiduciary capacity must be kept separate from those of the bank itself, and those of each trust separate one from another.

### **Investment of Funds**

Trust funds are invested according to the provisions of the will or deed under which they are held or, in the absence of specific directions, according to state law. Discretionary power of investment may be lodged with the bank. Investments left to the discretion of the trust department of the National City Bank of New York are made with the approval of a special committee of the bank's board of directors. When no special direction is given as to investment, trustees in New York are required to invest in securities which are legal investments for the funds of savings banks. A list of such securities is prepared at intervals by the state banking department.

When a client desires to free the trustee from this limitation, this wish is stated in the will or deed. Frequently

the donor gives very broad powers of investment to the trustee bank, permitting it to retain investments in the form in which the estate or trust is delivered and relying upon it to exercise its absolute discretion in the selection of securities when reinvestments are necessary. When the donor is living it is frequently provided that he shall be consulted as to new investments. Under trusts from courts, investments are generally made with the approval of the court unless the court by general order gives authority or the law covers investments by fiduciaries, as is the case in New York.

The trust department of a national bank may not receive deposits of current funds subject to check, bills or items for collection or exchange. No loans may be made to officers or employees of the bank. Banks do not draw wills or legal papers. In the state of New York it is unlawful for a corporation to practice law or give legal advice.

### **Kinds of Trust**

Each trust presents peculiarities of its own. Individual service is a characteristic feature of all trust work, hence the work of the trust department does not lend itself to ready classification. Some of the more frequently used forms of trusts may be considered.

Trusts may be divided along general lines into two classes: corporate, and individual. Corporate trusts include those activities carried on in connection with the financial affairs of a corporation. Corporate trust work has developed until it extends to practically every financial need of large business enterprises, including as it does, acting as trustee under mortgages and similar agreements; as depositary under escrows and reorganizations; as paying agent for dividends, coupons, and the principal of bonds and notes, as transfer agent and registrar of stocks, bonds, and notes, and as receiver, fiscal agent, and attorney.

For an individual the bank acts as trustee under voluntary trusts made by a person during his lifetime, for a specific purpose, such as the support of a relative, a charity, or the education of children. A bank may be executor of a will and also serve as trustee of funds left under it after the settlement of the estate. It may act as administrator by court appointment at the request of heirs when there is no will, or as guardian of the property of minors. The bank may also care for securities, relieving the holder of responsibility for their safe-keeping.

### Trustee under Mortgages

Since New York City is the chief market in America for floating bond issues, it is natural that a considerable part of the large New York bank's corporate trust activities should be devoted to handling trusts created by mortgages or trust indentures made to secure bond issues.

In a transaction of this sort the borrowers vest the trustee with title to property for the benefit of security-holders. The property involved may consist of securities, or of real estate or equipment; or it may be in other forms. If the assets pledged consist of securities the mortgage is described as a "collateral trust." The securities pledged are put in negotiable form or registered in the name of the trustee. The duty of the trustee is to carry out the provisions of the mortgages. If substitutions of collateral are permitted the trustee takes note that the security of the issue is preserved. Collateral trust mortgages usually provide that the borrowing corporation shall maintain a certain margin of collateral. In the interests of the security-holders, the trustee, if occasion requires, calls attention to this requirement. In handling mortgages other than collateral trusts the borrowing corporation retains possession of the property pledged, so long as it complies with the terms of the trust. In case of default under

either type of trust, however, it becomes the duty of the trustee to act in the interests of the security-holder in such manner as the mortgage may direct

In acting as trustee under mortgages securing bond issues, the bank takes custody of and makes deliveries of the bonds. The practice varies with the particular issue. In some cases the entire issue is to be delivered at the time the mortgage is executed. Frequently, however, deliveries are to be made in instalments, either periodically or when stated requirements have been complied with. The terms of a mortgage may require that prior bonds be retired out of the proceeds of the pending issue.

The trustee under a mortgage securing a bond issue, acts under the sinking fund provisions of the mortgage, if any exist. The proper amount must be set aside and disposition made of the fund. The mortgage may provide for retirement of a part of the issue by annual drawings, or may permit the retirement of a part of the issue at the option of the issuing corporation. In an instance of this sort the trustee arranges the drawings by lot and publishes the numbers called. In other cases the trustee invests the sinking fund instalment in interest-bearing securities for the benefit of the security-holders, or it may purchase a portion of the issue in the open market.

The final duty of the trustee in connection with mortgages securing a bond issue is to attend to the details of releasing the security to the borrower upon retirement of the issue. Under car trusts, equipment trusts, and similar liens, it is generally required that the borrowing corporation retire a portion of the issue from current earnings each year. Other mortgages require that the bonds be retired serially. When bonds are paid off, the release of the lien is recorded in the various places where the mortgage is on record and the retired bonds are canceled and destroyed.



### **Depository under Plans of Reorganization**

When a corporation defaults in its obligations it is obviously to the interests of the security-holders that the business be kept intact and that it be restored to a paying basis if possible. In other words, the security of mortgages based upon corporate property lies not only in the physical value of the property, but also upon its value in use by a going concern. Therefore it has become the custom to reorganize defaulting concerns, the reorganizer adjusts the claims of the various creditors and restores the business to a better financial standing.

In reorganizing a corporation a reorganization committee, consisting of a few of the principal security-holders, is formed. All security-holders are then called upon to deposit their holdings in trust pending the formulation of a reorganization plan or other concerted action to protect their interests. The trustee delivers to the holders temporary receipts for the securities surrendered, afterwards it delivers permanent receipts which are negotiable on the exchange upon which the issue is listed.

The trustee bank frequently assists the reorganization committee in preparing the plan of reorganization. Its main task, however, is to carry out the provisions of the plan. In performing such work the trustee collects assessments required and after the plan is completed it delivers new securities upon surrender of the trust receipts.

### **As Receiver**

Not always does it appear feasible or necessary to reorganize a company which is in financial difficulties. A device often used to restore the financial standing of such a concern is to have the court appoint a receiver to take charge of the concern's affairs. In acting as a receiver the bank exercises only the specific powers delegated to it by the court.

### Voluntary or Living Trusts

Modern trust service finds its most elastic and popular appeal in the voluntary or living trust. Under such a trust the donor transfers title to property to a trustee and instructs the trustee how to pay the income and reinvest the funds. The bank collects the income, invests and reinvests the principal, and at stated intervals accounts for its acts.

This form of trust may be made revocable and subject to change, or irrevocable and beyond the further reach of even the donor himself. It may be so drawn as to make a will unnecessary, or if but a part of the owner's property is placed in trust his will need dispose only of the remainder. Such a trust may be used to set aside a fund to educate children, provide for dependent relatives, insure regular payments to a designated charity, or, in fact, to safeguard funds of any amount with provision for the payment of income to himself or others, as the donor may desire. Many people are finding it desirable to leave life insurance in trust so that it may be safely and permanently invested for those for whose protection it has been provided.

A voluntary trust may be made the means through which a man who desires to retire from active business life obtains for making his investments the services of men still in close touch with market activities. He may for a small fee enjoy freedom from financial worry while enjoying the full fruits of his labors.

### Executor and Administrator

As executor named in a will, or as administrator of an estate under appointment of court where there is no will, the trust department takes charge of property, files an inventory with the court, pays funeral expenses and other just claims, finally distributing the property to those entitled to receive it. Sometimes the wife or husband or a business associate is

named as coexecutor. Inasmuch as the trust department already has deposited security with state authorities, it is not required further to bond itself as executor of the will. The estate therefore saves the charge which an executor ordinarily would incur in furnishing bond.

If the maker of a will desires he may place the will with the trust department, leaving the bank's receipt for the same among his papers to show that a will has been executed. As administrator the bank exercises the specific powers delegated to it by the court, dividing the estate among the heirs in the proportions fixed by law. After distribution of the property the administrator makes an accounting to the court and obtains his release just as does one who is serving as an executor under a will.

### Service Charges

The statutory fees for a trustee and executor in the state of New York are 5 per cent on amounts not over \$1,000,  $2\frac{1}{2}$  per cent on additional amounts not over \$10,000, and 1 per cent on all sums over \$11,000, on principal and at the same rate on income. In case there is more than one trustee and the amount involved is less than \$100,000, the commission at the usual rate is to be apportioned equally among them. On amounts of more than \$100,000, however, each trustee up to three is entitled to full legal fees. One-half of the commission is payable when the principal is placed in trust, and the remainder when the principal has finally been paid out.

Fees for the custodianship of securities vary widely according to the service performed. As will be shown in the following section this service may be merely the safe-keeping of securities or it may include a large number of duties, such as collecting coupons and dividends, preparing income tax certificates, reinvesting funds, giving information as to called bonds or conversion rights, etc. Commissions to be paid for

living or voluntary trusts, especially when large amounts are involved, are usually fixed by agreement. There is no fixed statutory charge for acting as depositary under escrow or similar agreements.

### **Custodianship of Securities**

According to the particular arrangements in effect with each customer, the extent of the bank's service in connection with custodianship of stocks and bonds varies from the mere safe-keeping of securities to the performance of all the details attendant upon ownership. Investors may find any or all the following advantages in entrusting their securities to the care of the bank.

- 1 The bank has special fire- and burglar-proof vaults in which the securities are kept

2. By having his securities stored near the exchange and in "good delivery" condition the customer can take advantage of the trading facilities of the bank to sell in a favorable market, if he cares to do so

- 3 The bank looks after collection of interest and dividends, relieving its customers of these business details

- 4 Convenience is also greatly served by using the department to hold securities for syndicates, for securing overdrafts of foreign banks, acceptances, etc

- 5 The bank keeps in touch with new developments concerning securities, such as, rights to subscribe to new issues, conversion privileges, bankruptcy proceedings, etc., and brings them to the attention of the owners.

### **Securities Received Book**

All securities taken for safe-keeping are entered in a securities received book consecutively in the order of their receipt. These entries show the numbers of the securities, the names of the registered holders of stocks, titles, maturities, and

interest periods of bonds; the total par value involved; from whom received and for whose account, and the bank's reference number. The securities received book is thus a book of original entry from which postings are made directly to the securities ledger to be described presently.

When securities have been approved by the department and entered in the proper records they are filed in the vault. The holdings of each customer are placed in separate envelopes. These envelopes are filed alphabetically in three sections—individuals, banks, and foreign customers.

### Nominees

As has been already indicated, the owner may make arrangements with the bank whereby it relieves him of the details and formalities attendant upon ownership. In order better to accomplish this purpose it is the customary procedure for the bank to have stocks transferred and bonds registered in the name of one of the members of the customers' securities department who is termed a "nominee." The nominee is to all intents and purposes the owner of the security and as such he has full powers to transfer title, to collect income, exercise rights, etc., without requiring specific authority for each transaction from the actual owner. Accordingly the bank is in a position to perform the routine function of collecting income without troubling the owner, while in selling, exercising rights, etc., the customer may communicate with the bank by letter, telegram, or cable and the bank can promptly execute his order.

### Changes in Status of Securities

One of the most valuable and at the same time exacting features of the customers' securities service consists in informing the owner of changes in the status of his securities and executing his orders in connection with the same. The daily papers and financial publications are read closely for notices

of calling bonds, reorganizations, receiverships, issues of new blocks of stock, expiration of conversion privileges, etc., and whenever such information comes to the attention of the department its total holdings are carefully checked to ascertain whether any customers are interested in the new developments. In the matter of reorganizations, receiverships, etc., the bank procures copies of the proposed plans and forwards them to the customers who are interested, at the same time asking for their instructions.

Frequently when new issues of bonds and capital stock are put out by railroads and industrial corporations, inducements are offered to the stockholders of record on a certain date to subscribe to the new issues. These "rights" as they are termed, may or may not be of much value depending upon the market for the new issue. Immediately upon receiving a notice of such act on the part of a corporation the department forwards the information to the customer concerned, and if he desires to take advantage of the "right" and purchase additional securities the bank executes his order. Stock issues may be paid for either in full or by instalments, in the latter case a careful record is kept of all payments made and the due date of others. In case the customer desires to sell his "right" the bank handles this phase of the work for him, provided a market can be found.

### Collection of Interest and Dividends

An important part of the customers' securities service consists in collecting and accounting to the customer for the income from bonds and stocks held by the bank. On making the bank custodian of his securities it is usual for the owner to give the bank full powers and instructions to collect and dispose of income and to prepare the income tax certificate which the government requires of all owners.

In collecting interest from coupon bonds the securities

ledger, which is to be described presently, serves as an interest tickler, showing the dates upon which coupons from all issues held in the department mature. Each month the ledger is inspected and a list of the coupons to be clipped and collected is prepared. The coupons are then clipped, counted, proved, and recorded in a coupon book. The coupons are also enclosed in collection envelopes, which are the same as those mentioned in connection with the work of the coupon collection department. Then they are routed through the incoming registered mail department to the coupon collection department in keeping with the interdepartmental arrangement of routing all coupons for collection through the former department.

Many registered securities are held merely for safe-keeping. Such are registered in the names of the owners, and the debtor corporations send checks covering interest or dividends direct to them. If, on the other hand, the bank has instructions to collect income from registered securities, the securities are registered in the name of the bank's nominees who then receive the dividend and interest checks from the debtor corporation. In the case of dividends on stocks which are not necessarily paid on any fixed date, the bank has the duty, of course, of watching for notices of dividends declared and making sure that transfers to its nominees have been made for all stocks upon which it is to collect the income before the transfer books of the debtor concern close.

### Disposition of Securities

Securities are surrendered only upon the explicit instructions of the owners. Withdrawals may be made for various reasons. The customer may desire that the securities be returned to him or he may order the bank to sell securities or to deliver them to a broker or a bond house for sale. Customers which are national banks often request the bank to forward United States government bonds to Washington

to secure new circulation Member banks of the federal reserve system located in the New York district may instruct the bank to deliver securities to the New York Federal Reserve Bank to be held by the latter as collateral for loans and other undertakings. Member banks located in other federal reserve districts may pledge securities held in New York with the federal reserve banks of this district In some cases this necessitates actual shipment of the securities to the pledgee bank Most frequently, however, arrangement is made for the New York bank to hold the collateral as agent for the pledgee

Finally securities may be pledged by customers to secure loans negotiated through the loan department of the bank Although the securities themselves pass out of the control of the customers' securities department if they are held in the name of a nominee, they are not removed from the records and a check on the collection of interest and dividends is kept for the benefit of the customer.

Before surrendering securities the signature of the owner's letter is verified in order to make sure that instructions are authentic. In case delivery is to be made over the window the person receiving the securities is required to furnish proper means of identification If delivery is to be made to the one who originally lodged the securities with the bank for safe-keeping, the receipt which the bank gave him when it received the securities may serve to identify him sufficiently In case the delivery is made to a person other than the one originally placing the securities in the custody of the bank, however, the receipt is not often available and complete identification becomes essential

Securities which have been disposed of are entered in the securities delivered book This book, like the received book, is a book of original entry, postings being made from it directly to the securities ledger In the securities delivered



book a record is kept of the following: the number of the stocks or bonds delivered, their disposition, total par value, to whom delivered, for what account, and a reference number. For accuracy, two persons are required to witness the withdrawal and to initial the corresponding entry in this book. In this way a check is maintained on the handling of all securities and responsibility for the withdrawal is fixed.

### Buying and Selling Orders

Mention has already been made of the service which may be rendered to customers in executing their orders to buy and sell securities. This service is of such importance that it merits special consideration. Wherever possible the orders are put into the hands of the bank's affiliated bond house, otherwise they are executed by stock brokers. In this way the customer receives the advantages to be derived from the bank's close association with its affiliated institution.

Orders for the purchase and sale of securities are entered in a buying and selling register. Here are entered the date upon which the instructions are received, the number of shares, a description of them, the limit price (if the instructions fix a limit), the owner's name, and the date when the order was executed. Upon the completion of a transaction the customer is advised that the securities are being held for his account in the case of a purchase, or that the proceeds have been credited to his account in the case of a sale. Then the items are closed out of the register. At any time, therefore, the total buying and selling orders which the bank has outstanding for its customers are represented by the open items in the register.

On account of the great volume of business transacted through brokers it is necessary for the bank to keep its records constantly reconciled with theirs. The original confirmation of purchases and sales received from brokers are carefully

checked against the register. The monthly statements of outstanding orders furnished by each broker are also proved against the buying and selling register. In this way the bank makes sure that the customers' orders are correctly executed.

### Books of Record

The records maintained by the customers' securities department, in addition to the received and delivered books, the coupon book, and the buying and selling register already described, consist of the stock number book, the temporary withdrawal book, the transient book, and the securities ledger.

*Stock Number Book* The function of the stock number book is to give a record of all stocks held, classified by issues. Each page is headed with the name of a particular issue. In making an entry, the date, the number of shares, and the name of the customer for whom the shares are being held, are recorded, as well as the original numbers of the shares, the person in whose name they were formerly registered, the new number, and the name of the person who has been appointed to act as nominee. When dividends on a particular issue are paid the bank readily ascertains from this book the names of the customers who are to receive payment. In this way the book serves as a check on all dividend payments which should be made to the bank for credit to customers' accounts.

*Temporary Withdrawal Book* The purpose of this book is to record all securities delivered to be received back again, that is, not passing permanently out of the bank's possession. These temporary withdrawals occur for such reasons as: the exchange of interim certificates for definitive bonds, the conversion of one issue into another, change of a coupon bond into a registered one, or vice versa, transfer of stock, etc. When securities are withdrawn temporarily, entries giving a description of the securities and reasons for withdrawal are made. When items are returned these entries are stamped out.

HELD FOR ACCOUNT OF <u>Farmer and Mechanics National Bank</u>									
<u>First North Texas</u>									
DATE MATURITY INCOME PAYABLE									
TITLE OF BONDS <u>American Telegraph &amp; Telephone</u> <u>6 2 1/2 1924 m/n</u>									
DATE	OPEN CREDIT	AMOUNT DEBITED	AMOUNT CREDITED	CHECKED BY	BALANCE	TEMPORARY WITHDRAWALS AMOUNT	DATE RETURNED		
3/21/21					10,000.00				
4/6/21	742	5,000.00		Am	5,000.00				
4/10/21	816	4,000.00		Am	1,000.00				
4/12/21			9,000.00		10,000.00				
5/2/21					5,000.00				
6/11/21			10,000.00		20,000.00				
6/15/21	822	11,500.00			9,500.00	5,000	5/10/21		

Form 81. Securities Ledger. (Size 11 x 8)

of the book Every few days the book is examined to make sure that the securities have been returned to the bank in due course

*Transient Book.* Frequently securities are received to be held only temporarily, as, for example, when a customer sends stock to be transferred and returned to him Securities of this sort are entered in the transient book This book contains space for entering the same information as that contained in the securities received book, and in addition space is provided for recording the reason for which the securities were sent to the department When the securities are returned the entries are closed out of this book

### Securities Ledger

The securities ledger (Form 81) is a book of final entry showing the amount of securities held for each customer Each page is headed with the name of a customer and is divided into horizontal sections, one for each issue of stock held for him The sections contain space for the number of shares received from the customer and the number delivered, together with the balance.

## CHAPTER XX

### THE BANK AS REGISTRAR AND FISCAL AGENT

#### Transfer Agent for Corporations

Functions which require close fiduciary relations are those whereby the bank acts as transfer agent and registrar for certain of its client corporations

In acting as transfer agent the chief duty of the bank is to perform the routine matters connected with transferring ownership of shares of stock. Ownership of stock is represented by certificates, which may be for any number of shares. These certificates are not negotiable in the ordinary sense, rather, ownership to the shares of stock which they represent is transferable on the books of the corporation by assignment. Following is a form of assignment used for this purpose:

For value received . . . hereby sell, assign and transfer unto . . . shares of capital stock represented by the within certificate, and do hereby irrevocably constitute and appoint attorney to transfer the said stock on the books of the within-named company, with full power of substitution in the premises

Dated.

In the presence of

Signed

As has been indicated the essential requirement for a transfer is that the transaction be recorded on the books of the issuing corporation. The old certificate bearing the duly executed assignment of the stockholder is presented to the issuing corporation or its agent. Here the proper entry is made on the transfer books of the corporation and a new certificate or certificates issued to replace the one assigned.

It is proper, and in the case of small corporations it is the usual practice for the corporation to act as its own transfer agent. The stocks of many of the larger corporations are actively traded in on the New York Stock Exchange, thereby necessitating a large volume of transfers. By custom, corporations whose stocks are listed usually maintain transfer agencies in the financial district of the city. Many corporations of this class, however, do not consider it advisable to locate financial offices in the vicinity of the Stock Exchange and to maintain the specialized clerical forces necessary to make their transfers, hence they designate some bank or other financial institution to act in this capacity.

#### **Information Filed with Transfer Agent**

When the bank accepts an appointment to act as transfer agent for a corporation, it requires certain important information to be furnished. This usually consists of

- 1 Specimen stock certificates in the form adopted by the corporation
- 2 Specimen signatures of all officers of the corporation authorized to sign or countersign stock certificates
- 3 A copy of the charter or certificate of incorporation of the corporation, with all amendments to date, duly certified by the state officer having custody of the original thereof
- 4 A copy of the by-laws of the corporation as at present in force, duly certified by the secretary or clerk of the corporation under its corporate seal
- 5 A similarly certified copy of the resolutions appointing the bank transfer agent for the corporation

#### **Duties of Transfer Agent**

As transfer agent the transfer department of the bank becomes the custodian of the stock books of the corporation,

which include the stock transfer book and the stock ledger, together with a supply of blank stock certificates. The stock certificates are numbered consecutively and are signed by the proper officials of the corporation before they are delivered to the transfer agent. They are not valid, however, unless countersigned by the transfer agent and the registrar. It is the duty of the transfer agent to pass upon the regularity and legality of the assignment of the title to the certificate, enter a record of the transfer on the books of the corporation, cancel the old certificate, and execute and deliver the new one.

### **Examination of Stocks Offered for Transfer**

In receiving stock for transfer the examination necessary to establish the fact that it is in proper condition for transfer is made at the window in order that any irregularities may be immediately brought to the attention of the bearer. The genuineness of the certificate is established by means of the signatures of the proper officers of the issuing corporation, the transfer agent, and the registrar. The assignment of the certificate on the reverse side is examined to make sure that such assignment has been properly executed. A notice appears on the back of the certificate as follows. "The signature to this assignment must correspond with the name as written upon the face of the certificate in every particular without alteration or enlargement or any change whatever." The examiner makes sure that this provision has been adhered to. If the signature is not known to the bank it is required to be guaranteed by some bank in the city or having a correspondent in the city, or by a member of the New York or Boston Stock Exchange. Signatures of members of these exchanges are kept in a card file accessible to the window clerk.

Before certificates can be accepted for transfer it must be ascertained that no stop-orders have been lodged against them. The owner of a certificate may request a transfer to

be stopped in the case of loss or theft or other contingency. The transfer may also be stopped by order of the court. In order that stop-orders may be readily referred to, the bank keeps a card file of these orders accessible for the examiner. In this connection it might further be stated that the usual time for issuing new certificates in place of those lost or stolen is one year after notice of the loss has been given, and then only after the loser has filed a bond of indemnity for twice the par value of the stocks, or even more in some cases.

### **Delivery Receipts**

Time is required to cancel the old certificates, issue the new ones, and make the necessary entries on the books. For this reason the bank has the customer leave the transaction in its hands overnight and it issues a numbered receipt in exchange for the stock delivered. To each receipt there are two sections: one held by the owner of the securities, the other by the bank. On calling for his securities the owner establishes his identity by means of this receipt. The bank's section of the receipt is attached to the stock certificate to insure its being readily located for delivery to the owner.

### **Checks Against Overissue**

To replace the surrendered certificate, the transfer agent issues a new one, using from its supply of blank certificates the one bearing the lowest serial number. The canceled stamp is then placed on the old certificate. As a check upon this work the auditors of the bank prove the old certificates against the new ones and submit the latter to an officer of the bank for signature, then they send the new and canceled ones to the registrar of the issuing company in order that he may register them. After the certificates have been returned by the registrar the new ones are delivered upon the surrender of the receipt. The canceled certificates are filed as a record.



### Stock Transfer Book and Ledger

Original entry of the transfer is made in the stock transfer book of the corporation. Each sheet of this book is ruled to contain the date, the name of the assignor, the number of the certificate canceled, the number of shares involved, the name and address of the assignee, and the number and amount of new certificates issued. In the event the corporation is not domiciled in New York it usually maintains another set of transfer books in the state in which it was incorporated. In order that the home office of the corporation may have complete information as to the ownership of its shares, the New York transfer agent usually sends duplicate copies of the transfer sheets to it.

A stock ledger is maintained for each concern for which the bank acts as transfer agent. The stock ledger is designed to show the name of each stockholder of the corporation and the amount of his holdings. Accordingly there is an account with each shareholder. The title space of the account contains the stockholder's name and address and the disposition which he wishes to be made of dividends as they are declared. Entries to the stock ledger (Form 82) are made from the sheets of the stock transfer book. The debit side of the ledger shows deductions from the amounts owned. Here are entered the date of surrender, number of certificate surrendered, and number of shares represented. The credit side of the ledger accounts show accretions to ownership. Here are entered the date of issue, the number of new certificates, the number of shares involved, and the balance held by the stockholder.

### Registration of Stocks and Bonds

Enough has been said in connection with stock transfers about the method of issuance of new certificates of stock to indicate how important it is that some control be placed over



the amount issued and the circumstances under which such issue takes place. The appointment of a responsible transfer agent is, of course, a long step in this direction. The activities of the transfer agent, however, constitute mainly a protection for the corporation against forgeries, fraudulent transfers, etc. The public—those who deal in stocks for investment—also has an interest in the matter, however. It is interested in knowing that stock certificates represent stock issued strictly in accordance with the authority of the director of the issuing corporation. Hence it has become a practice well-nigh universal for a corporation to employ some disinterested third party, such as a bank, to act as registrar for its stock. In fact, registration is an operation essential to validity in the case of securities traded in on the New York Stock Exchange.

### **Duties of Registrar**

The relations between the corporation and its registrar are usually contractual. This contract defines the liabilities of the registrar since there is no law specially fixing this liability and few court decisions on the matter.

In acting as registrar for the stock of a corporation it is the duty of the bank to see that the amount of stock issued does not exceed the amount authorized by the corporation. When issuance of the certificates is first made and when similar ones are issued to cover additional authorizations, the bank compares the number of shares represented by certificates with those authorized, and if it finds everything to be in order it registers the certificates in the book kept for that purpose and places its signature indicating approval on the stock certificate. In the case of shares already outstanding, the duty of the registrar consists of making sure that a valid certificate, or certificates, representing the same amount of shares to be canceled for each new certificate issued by a transfer agent or by the corporation itself.

### Acting as Registrar and Transfer Agent

The registrar thus acts as a check upon the work of the transfer agent. While the same department of the bank acts both as transfer agent and registrar, it must be borne in mind that it cannot perform these services for the same corporation. For one group of corporations it acts as transfer agent; for another, as registrar of stocks.

### Routine of Registration

When the new and canceled certificates are received either from the company itself or from its regularly appointed transfer agent, a thorough examination of the certificates both old and new is made. If everything is found in order, record of the certificates is taken in the stock register which gives the date, numbers of certificates and amount of shares canceled, and the numbers of certificates issued instead, the number of shares to be registered, in whose name issued, and the date of issue. The cancellations are proved against the issuances, that is, the ledger is examined to make sure that only the authorized amount of stock is outstanding on the books. As a final step the registrar places his canceled stamp on old certificates and validates new ones by means of his signature. Both certificates are then returned to the transfer agent for delivery.

### Registration of Bonds

In addition to its work as registrar and transfer agent for stocks, the bank may act as registrar for the bonds of corporations. This activity is similar to acting as transfer agent rather than to that of acting as registrar for stocks. Bonds are of two kinds—registered and coupon. Title to the latter class passes by delivery. The owner collects his interest by detaching and presenting for payment the serially dated coupons attached to the bond, as they mature. Because of

the ease of passing title this type of bond is preferred by those who deal extensively in bonds and who have ample facilities for their safe-keeping. In connection with some issues of bonds, however, provision is made for floating a portion of the issue in registered form or for the exchange of coupon bonds for registered ones. The registered bond differs from the coupon bond in that title is passed on the books of the corporation in much the same way as stocks and that interest is paid by mailing a check to the registered holder. Some issues of bonds are registerable as to principal only, however. In a case of this sort title to the principal amount of the bond is passed on the books of the issuing corporation, while interest is paid by means of coupons.

As in function, so in practice, the operation of registering bonds is similar to that of transferring stock. When a bond is presented for transfer and registration an irrevocable power of attorney is executed similar to assignment found on the back of stock certificates. In registering bonds the procedure differs from that of transferring stock, however, in that new bonds are not issued for the ones surrendered. The same bond is used for both the assignor and the registered holder, change of ownership being indicated by writing on the back of the instrument. Accordingly, on the back of the bond a space is ruled for the date of registration, the name of the holder, and the signature of the official of the bank who acts as registrar.

### **Books Used for Bond Registration**

The following books are used in transferring and registering bonds

1. The transfer book, which contains the names from which and to which the bonds were transferred, the bond numbers (if coupon bonds), the number of the coupon next due, the ledger folio number

of the account, and whether the bonds were received by registered mail, express, or over the window

2. The index, containing the names and addresses of all registered bondholders to whom the registered interest is to be paid
3. The ledger, in which is recorded the names of the registered bondholders, the bond numbers, the dates on which the bonds were registered, the dates on which they were transferred out of the account, and the total amount of bonds registered for each holder.

### Payment of Registered Interest

The bank may or may not pay the interest on the issues of bonds for which it acts as registrar. At the request of the corporation the bank may furnish it with a list of the fully registered bondholders and the checks for the interest may be mailed direct from the corporation's office. However, the corporation may send the bank a check for the total amount of the registered interest and have the bank mail checks to the registered bondholders in accordance with the mailing orders on file. Such a check would be credited to a special account and the checks which the bank sends would be charged to this account as they are returned and paid. Before mailing the checks the bank requires that a properly executed income tax certificate be filed with it in each instance. To facilitate this a form letter is mailed about a month before the interest is due, enclosing the proper certificate and requesting that it be duly executed and returned to the bank one day prior to the date on which the interest is due. After the checks have been mailed the bank sends the corporation a list giving the names of the registered bondholders, the total of the bonds held by each, and the total amount of the checks mailed.

### Payment of Dividends

The transfer department may be called upon to pay dividends upon the stock issue which it transfers. Sometimes a list of the shareholders and the number of shares held by each is sent to the corporation, which in this case attends to making the payment.

### Closing Transfer Books

Some corporations close their transfer books some time prior to paying dividends. This is done for the purpose of enabling the transfer agent to prepare the necessary lists of stockholders. At the time of declaring the dividend the corporation fixes the date of payment and the last date for transferring stock in order to participate in the distribution. From the transfer books the transfer agent prepares a list of the stockholders as of the closing date, and makes payment to the persons whose names are contained in the book, or furnishes the list to the corporation, according to instructions received.

### Subscriptions to Stock

The transfer department also receives subscriptions for the increase of capital stock of a corporation. In most cases the subscriptions are payable in instalments, when payments are made they are noted on the back of the instalment receipts issued to subscribers. A record is kept in a ledger showing the amount paid in for each account, also the total amount received each day. The aggregate amount of cash and checks received each day is proved against the subscription receipts; the cash items are sent to the note teller and the account of the corporation credited for the amount. In case shares are issued before they are fully paid the certificate states that such and such instalments have been paid and the later payments are indorsed on the back.

### Compensation of Bank

There are various ways in which a company pays its transfer agent and registrar, sometimes the contract drawn provides for the payment of a certain amount for each certificate registered and for each one transferred. One common arrangement is for the two parties to enter into a yearly contract by which for a fixed total sum the transfer agent agrees to do the transfer work irrespective of the number of certificates presented. The company bears the expense of engraving and providing new certificates. The sums charged vary with the volume of the work, which in turn depends upon the following factors: the number and kinds of services undertaken, the number of shares and of stockholders, the activity of the shares, the frequency of dividends, and whether the bank sends out the dividend checks, etc. But whatever amount is agreed upon, the corporation pays in addition expenses for postage, envelopes, etc. The transfer agent assumes greater responsibilities than the registrar and his compensation is accordingly larger.

### Transfer of Bank's Own Stock

The transfer department also acts as transfer agent for the capital stock of the bank itself. Dividend checks are mailed through the department and all transfers of stock are made here, the same records being maintained for the bank's own stock as are kept for that of any corporation. In connection with its transfer activities for the bank, the department handles the proxies of those stockholders who cannot be present at the annual meeting.

At a reasonable interval before the annual meeting of the stockholders takes place there is mailed to each stockholder a proxy with a letter attached informing him of the date of the meeting and requesting him to sign the proxy and return it to the department if he cannot be present. These signed



proxies when received are sorted according to the ledger and the number of shares held by the owner entered at the top of the proxy. They are held until the day of the annual meeting at which time they are turned over to the officers of the bank.

### **Bank as Fiscal Agent**

In the description of the work of the coupon collection department of the bank, mention has been made of the fact that the great bulk of the interest due on securities issued by American corporations and on those foreign securities which are held in the United States is paid in New York City. Through the correspondent bank system, coupons from bonds held by investors throughout the United States and the chief investing countries of the world find their way into New York City for payment. In addition, matured bonds are forwarded for collection through these channels.

To meet obligations of this sort, debtor corporations, governments, and municipalities may set up and operate their own paying offices. For the convenience of collecting banks and investors, however, it is a common practice to appoint a bank or trust company located in the financial district to act as fiscal agent. Usually a debtor concern selects the bank with which it keeps its commercial account to act in this capacity.

### **Methods of Providing Fiscal Agent with Funds**

The arrangements between the client and his fiscal agent vary with each individual case. In many instances the funds needed for making the payments are deposited in the bank in a special account known as "Funds Deposited to Pay Bonds and Coupons." In other cases the client may provide funds by authorizing the bank to charge payments of matured bonds and coupons to his regular deposit account or to the account

of some other bank or organization with which it has made previous arrangements.

When asked to make payments arising from an issue of bonds, the bank obtains a specimen of the bond and coupons or a detailed description of them together with specimens of the signatures appearing thereon. This information is used in passing upon the validity of bonds and coupons presented for payment.

The arrangement with regard to income tax returns and deductions required by the national law is an important point to be settled preliminary to establishing fiscal agency relations between bank and client. Some concerns attend to this work themselves while others have their fiscal agent do it. In the latter case the bank requires the client to furnish a letter of indemnity protecting it against any claim which the federal government may make against it by reason of its making unavoidable errors.

### Incoming Coupons

Coupons presented for payment are usually enclosed in the paying agent's own particular style of envelope. For this purpose the various banks of the city which handle quantities of coupons keep on hand a supply of envelopes furnished by the paying agent. This envelope shows the name of the issuing company, number and amount of coupons enclosed, and the total amount. Time is required to make examination of the material presented for payment and to issue the necessary check, hence payment is not made immediately upon presentment. The bearer of the envelope containing coupons is given a numbered identification receipt. The number of this receipt is stamped on the coupon envelope and serves to distinguish the transaction from others in process. Later the bearer exchanges his receipt for a coupon check covering the amount.

### Approval for Payment

Coupons presented for payment at the bank are carefully counted to see that the amount enclosed agrees with the total shown on the outside of the envelope. They are also scrutinized to see that they are payable at the bank, that they are due, and that the proper ownership certificate is attached. Stop-payment orders may be lodged against coupons, hence the bank watches for this defect. When all is found to be in order for payment a distinctive form of cashier's check, the "coupon check" mentioned above, is drawn up and delivered to the bearer upon surrender of his receipt.

### The Coupon Sheets and Returned Book

After payment has been approved, the transactions are entered on the coupon sheets which give the number of the check issued in payment, the name of the coupons paid, the total amount, the net amount paid, and the total of the check for all issues paid to any one customer. This is done so that the totals of the coupons received may be proved with the totals of the payments listed on the sheets.

The paid coupons are to be returned to the debtor concern as paid vouchers. They are accordingly transferred to larger envelopes upon the outside of which appears a list of the contents. From the envelopes, entries are made to the coupons returned book. This book classifies coupons paid according to two categories—those which have been charged to the "Funds Deposited to Pay Coupons" account, and those charged to other accounts. At the close of the day the total charges posted in this book are proved against the coupon sheets and the total checks issued. This book accordingly serves as a proof book over the coupon-paying operations. After entry has been made to this book the canceled coupons are sent to the auditors who examine them and forward them to the customer.

### Coupon Ledgers

As has already been indicated, payments made by the fiscal agent are charged either to a special Funds Deposited to Pay Coupons account or to one of the regular deposit accounts of the bank. Charges made to the latter accounts are sent to the bookkeepers of the bank in the form of charge tickets. To contain a record of the state of the Funds Deposited to Pay Coupons account, a coupon ledger is maintained. In this ledger appears the Funds Deposited account of each concern which deposits funds for this purpose. When funds are received, credit is made to the Funds account of the sender in this book. Likewise, from the coupons returned book, payments made are posted to the debit side of the Funds account of each customer. In this book there is also a control account over the various special accounts of the department.

### Normal Income Tax

Under the United States income tax law a debtor corporation may pay for its security-holders a tax at the rate of 2 per cent on the income paid them. It is optional with the borrowing corporation whether or not it will assume this 2 per cent tax. To make security issues more attractive to investors, however, borrowing corporations in increasing numbers insert a so-called tax-free covenant clause in the agreements covering new issues of securities. Corporations, governments, and municipalities domiciled outside the United States are not permitted to assume the normal tax.

In collecting the income from a tax-free issue of securities the owner indicates by the use of the proper form of income tax return whether he is exempt from federal income tax or not. Should the owner claim exemption, the corporation of course does not have to pay any tax for him. In case the owner does not claim exemption from the tax, however, the debtor corporation pays the owner at the full coupon rate of

his securities and in addition it pays the government 2 per cent of the amount paid the owner. In paying his income tax the owner of such securities is permitted to deduct from the gross amount of tax due, the amount paid for him "at the source," as the payment of 2 per cent paid to the debtor corporation is termed.

### **Tax Collected by Non-Resident Aliens**

A portion of the income tax law which affects the debtor concern or its fiscal agent in a way similar to the tax-free clause is the requirement that the income tax assessed against citizens of foreign countries must be deducted and paid to the government by the debtor concern. Obviously the government of the United States has no authority over non-resident aliens to compel them to file income tax returns and pay taxes on incomes which they have collected, as it does in the case of residents of this country. The government meets this situation by requiring the debtor corporation to retain for the Collector of Internal Revenue at the time of paying income to non-resident aliens the full amount of tax due from them. From the owner's standpoint this arrangement differs from the tax-free arrangement in that the non-resident alien receives the gross amount of income less the tax collected, while the recipient of tax-free income receives the gross amount due him, the debtor corporation bearing the tax cost.

The debtor concern may or may not delegate to the paying agent the task of handling income tax deductions under tax-free and alien ownership requirements. It is a convenient and a common arrangement to have the agent do it. When the agent acts in this capacity it determines the amount to be paid the government from the ownership certificates filed by owners. Each month it makes disbursement to the government of the necessary amounts. Pending disbursement an account entitled "Federal Income Tax Due United States

Government According to Monthly Returns" is credited. The funds for making these payments may be obtained in any of the ways for obtaining funds to pay the coupons themselves.

In some cases under tax-free clauses these concerns send the agent an additional amount equal to 2 per cent on the entire amount of income on a given issue of securities, since it cannot be determined in advance how much of the income will be paid to owners who claim exemption from the tax. Remittances received in this way are credited to an account termed "Funds Held Awaiting Disbursement Account Federal Income Tax." This account is debited for credits made to the "Federal Income Tax, Due United States Government According to Monthly Returns" account in connection with the bond issue of the sender of the funds. After the whole of the income from the issue has been paid, the balance remaining in this account is returned to the client.

### Ownership Certificates

In addition to caring for the normal tax deductions, the debtor concern or its fiscal agent has the duty of forwarding to the government the ownership certificates submitted by holders of securities. Once a month the returns, which in the meantime have been carefully checked against the books and other records of the paying agent, are forwarded to the Collector of Internal Revenue. The collector requires the paying agent to submit reports on prescribed forms, showing details of the certificates forwarded. There are two of these forms—one contains a report on certificates in connection with which the paying agent has deducted or paid tax at the source, the other contains reports on all other income.

The purpose of these reports is to enable the collector to make sure that he receives ownership certificates covering the whole of the income disbursed, also to enable him to account for amounts withheld or paid at the source.

## CHAPTER XXI

### DOMESTIC BOOKKEEPING

#### Bank Accounting

The accounting work of the bank may be divided into four parts:

1. Preparing the original entry material
2. Keeping the accounts of depositors
3. Keeping the general books and preparing financial statements
4. Auditing.

#### Preparing the Original Entry Material

The work of preparing the original entry material is performed mainly in the operating departments of the bank as has been indicated in the discussion of the various operations. This work consists of sorting the material according to ledgers to facilitate posting, of proving the accuracy of the entries, and of preparing figures for the control accounts which the general bookkeepers maintain over the depositors' ledgers. Thus the receiving teller sorts his deposit slips, which are original entry material for credits to depositors' accounts, according to ledgers before he sends them to the depositors' ledger bookkeepers, and he sends a statement to the general bookkeeper showing the total credits sent to each ledger for the day. In like manner the mail teller reports the cash letters which he sends to the bookkeepers, the transit department its duplicate letters of transmittal, and the certification department its certifications. Following the same scheme of control, the single tickets representing credits to customers' accounts for collections, discounts and loans credited to their accounts,

etc., pass through departmental journals from which the proper proofs are prepared. In this way all original entry material passes directly from the operating departments to the bookkeepers, except the "double" tickets and the checks drawn upon the bank itself. The double tickets and the checks drawn upon the bank are then sorted, proved, and prepared for posting by specialized departments. The ticket journal department prepares the double tickets and the check desk or domestic bookkeeping department prepares the checks.

### **Ticket Journal Department**

The bookkeeping tickets used in the work of the bank may be either "single" or "double" tickets. A single ticket is always a credit ticket offset by a debit made through a departmental proof, while a double ticket consists of two or more tickets representing the debits and the corresponding credits arising from a given transaction. Single tickets are sorted and proved by the operating departments which maintain credit journals, as has been indicated above. Double tickets, however, which represent approximately 75 per cent of the entire amount of tickets written in the bank, pass through the ticket journal department the function of which is to sort, prove, and record such tickets.

Each operating department sends its double tickets to the ticket journal department as they accumulate in convenient volume. The tickets come to the latter department by entries, i.e., the ticket or tickets carrying the debits arising from a given transaction are attached to the ones carrying the credit offset.

As a first process in proving the tickets, the debits are compared with the credits to see that each entry balances. The tickets are next proved by the batch system. This is done by sorting them according to the ledgers to which posting is to be made and showing that the debits in a particular batch



equal the credits. The tickets for the general ledger are merely listed in total and sent to the general bookkeepers' department to be sorted, proved, and posted in the subsidiary ledgers. Those tickets which are to be posted to customers' accounts are listed in detail in duplicate. The totals charged and credited to each ledger are then entered on a batch proof form and the tickets are passed to the proper bookkeepers for posting.

The main function of the ticket journal department finds expression in the daily proof (Form 83) which classifies the total charges and credits arising in the bank from double tickets. This proof is a consolidation of the batch proofs prepared in sorting the tickets and serves to give to the general bookkeeper figures for his control accounts over the depositors' ledgers.

### Preparing Checks for Posting

The other class of items requiring a specialized department to prepare them for posting consists of checks and other items drawn upon, or payable at the bank. In sorting its bookkeeping material each operating department throws the checks drawn upon the bank together and charges them in bulk to the check desk department. These items are the "Eights" shown upon the illustrative forms. So far as the checks which come into the bank through the operating departments are concerned they might be sorted and charged direct to the ledgers and control figures sent to the general bookkeepers on the departmental proofs, just as the letters in the mail teller's work and the deposit slips of the receiving teller are credited to the ledgers direct. There is, however, an enormous volume of these checks entering the bank from the clearing house which cannot conveniently be included in the proof figures of some one of the operating departments. In addition to the work of proving these items from the clearing house

## DOMESTIC BOOKKEEPING

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DEBITS		CLERK	DATE	CREDITS	
TICKET JOURNAL				GENERAL LEDGER	
39,386.27	26			44,726.42	14
123,898.78				26,218.95	
799,608.52				72,675.71	
69,508.65				37,030.77	
65,011.52				36,779.41	
408.48				1,963.84	
7,432.82				122,118.57	
686.65				8,800.47	
1,246.78				10,584.39	
92,153.80				37,520.78	
22,576.10				44,821.88	
5,182.61				165,913.80	
1,616.93				29,664.66	
5,751.65				663,214.67	
14,378.36				46,782.22	
5,075.37				7,252.20	
257,227.99				7,952.93	
40,837.98	23			51,219.56	75
912,753.04				91,866.01	
567,222.43				279,203.00	
109,877.41				103,931.56	
180,542.19				1,039,676.97	
97,453.60				156,448.20	
405,123.28				257,539.20	
401,078.77				361,476.00	
2,674,746.22				2,291,120.74	
38,338.82				26,376.41	
373,821.16				253,241.27	
1,197,060.87				292,016.20	
296,364.86				3,006.36	
200,353.26				110,711.89	
2,126,138.95				685,752.13	
896,450.37				307,049.08	
711,367.36				541,075.72	
2,677,025.65				1,076,132.87	
344,560.83				618,481.06	
4,633,597.69				5,150,276.06	
9,205,061.81				7,992,929.79	
196,736.79				4,375.07	
494,621.46				219,912.72	
395,319.22				92,910.97	
21,898.58				14,239.40	
109,765.29				3,978.38	
897,286.79				2,967.47	
9,045.01				27,080.20	
1,365,526.97				1,176,926.46	
3,460,020.11				1,442,820.67	
13,128.68				27,773.85	
3,370,033.00				1,994,802.75	
12,186.55				191,346.47	
7,018,673.95				3,006,367.57	
375,868.81				103,760.59	
10,789,820.92				5,414,531.23	
69,093,340.31				69,093,340.31	

there is the task of passing upon whether or not the bank can pay them. Some may not be drawn upon the bank, others may have been listed incorrectly, others forged, raised, or irregularly indorsed, and stop-payment orders may be in effect against some. Furthermore, if the bank is to observe the clearing house rules for returning items and correcting errors this work must be done speedily and accurately. A maximum of efficiency is obtained by combining these incoming clearing house items with all other checks drawn upon the bank and setting up a specialized department to handle them. In accordance with this scheme the check desk department has the function of proving the whole mass of checks drawn upon the bank and preparing the items for posting by the bookkeepers. In conjunction with the bookkeepers and the signature control department the check desk also attends to the work of deciding which checks the bank should pay.

### Check Desk Department

In keeping with the inflow of its work the check desk department operates in two sections, or shifts, the morning and the afternoon. The task of the morning section is to care for the items brought back to the bank from the clearing house, together with any which the operating departments may send in time to be included. The material of the afternoon section is, on the other hand, the items coming to the bank through the various operating departments: the mail teller, the receiving teller, the foreign teller, the paying teller, the city collection department, etc.

### Proving Clearing House Checks

The checks received from each clearing house bank come enclosed in an envelope upon which the contents are listed. This amount constitutes the charge made against the receiving bank in the morning's clearings by the sender. The first

work is to prove the accuracy of these charges. In proving the incoming clearing house exchanges those checks received from each bank are proved as a batch. This is done by sorting the checks according to ledgers and proving that the total sorted by ledgers equals the total amount noted on the outside of the envelope. The checks for each ledger are then listed in detail and passed to the proper bookkeeping section.

### Claims and Allowances

This process of proving the checks locates errors occasioned by clearing house banks the sendings of which are incorrectly listed, or the checks of which are drawn on some other institution. When an error of this sort is detected the correction is made in the sending bank's list. In case the receiving bank has been overcharged the amount of the error constitutes a "claim" against the bank making the error. On the other hand, should the receiving bank be undercharged the amount becomes an "allow" to the sending bank. In either case the error is turned over to the city collection department, which makes the adjustment with the clearing house bank.

### Checks from Operating Departments

The operating departments constitute a second source of items for the check desk. Periodically these departments charge and send their accumulations of checks to the check desk. Each package is accompanied by an adding machine list of its contents. When a sufficient number has been received these packages of checks, or "banks," as they are termed, are sorted according to ledgers and the amounts sorted to each ledger are proved against the adding machine lists from the sending departments, just as are those received from clearing house banks. The checks are then placed with those from the clearings and from this point onward items from the two sources follow the same course through the department.

### Ledger Proof of Checks

After the checks have been sorted according to ledgers they are further subdivided according to accounts within the ledgers. For this work there is a force of clerks to handle the material for each ledger. Any given ledger force lists every check which has been sorted to its ledger, making a recapitulation of the entire charge for the use of the proof clerk in preparing the daily department proof. The checks are then sorted according to drawers' names. For each assortment there is made an adding machine slip showing the total charge to be made to the drawer's account for the attached checks. These totals, which are later used by the ledger bookkeepers as a basis for their entries, are then proved against the entire amount charged to that particular ledger.

### Drawn Against Demand Deposits

In addition to checks drawn against the demand deposit accounts of its domestic customers, the bank also receives through the check desk certain other items. These consist chiefly of drafts drawn by depositors in the foreign division, the bank's own acceptances, drafts drawn under letters of credit, travelers' checks, notes made payable at the bank by others than depositors, coupon checks, certificates of deposit, certified checks, checks drawn against time deposits, etc.

### Foreign Drafts and Acceptances

In disposing of the bank's own acceptances and drafts drawn by depositors in the foreign division the whole mass is charged in total to the foreign bookkeeping department, which keeps the accounts to which these items are to be charged. This latter department sends acceptances to the proper commercial credit department. The commercial credit department examines them and sends to the foreign bookkeepers those which are dishonored together with tickets show-

ing the account to which each of the paid acceptances is charged. The foreign bookkeeping department itself cares for the foreign drafts. These are sorted according to ledgers and those which are dishonored are returned to the check desk along with the dishonored acceptances. At the end of the day the foreign bookkeeping department prepares a proof of its receipts from the check desk. This proof shows the amount charged to each ledger and to the acceptance accounts, and it is used by the check desk proof clerk in preparing his proof of the day's operations.

Travelers' checks and drafts drawn under letters of credit are charged to the letter of credit department as they are received. Since the Travelers' Checks account is kept by the general bookkeepers the letter of credit department, after an examination of the checks to make sure they are correctly drawn, sends the check desk a ticket charging the Travelers' Checks account for the total amount of the checks. This ticket is then charged to the general bookkeepers according to a method to be described presently. Drafts drawn under letters of credit are also charged to the letter of credit department as they are received. At the end of the day this department forwards the check desk a ticket covering the total of the drafts which it will honor, the actual charges for the drafts being withheld until the following day in order to facilitate the work of the department. This ticket, then, representing a cash hold-over constitutes a charge to the city collection department, to which department all cash hold-overs of the bank are charged. The next day the letter of credit department sends to the check desk a ticket covering each draft received. These tickets charge either the general account "Cash Letters of Credit" if the credit was issued for cash, the general account "Advances to Customers on Letters of Credit" if the credit was guaranteed and the customer does not maintain a balance with the bank, or the customer's account

in the case of the guaranteed credit issued to a depositor. Accordingly the tickets are charged either to the general book-keeping department or the customers' bookkeepers by the check desk and these charges offset the charges made to the city collection department the preceding day.

### Notes of Others than Customers

Occasionally notes made payable at the bank by others than depositors are presented for payment. Obviously these cannot be charged to account. Drawers of such notes make arrangements to have them honored by placing funds with the note teller, giving him instructions to pay the notes when presented to the bank. Such notes when received at the check desk are charged and sent to the note teller. If funds have been received to pay a note the note teller pays it and returns it to the drawer. If no funds have been received, however, the note is sent back to the check desk to be returned to the sending bank in the usual way.

### Debit Cash Book

Coupon checks, certificates of deposit, cashier's checks, as well as the tickets used in connection with travelers' checks, letters of credit, and acceptances already mentioned, are drawn against accounts maintained by the general bookkeepers. They are accordingly charged to the general bookkeepers who make entries to the proper accounts. To keep a record of all charges made in this way a book known as the "debit cash book" is kept at the check desk.

### Certified Checks

Special mention should be made of the procedure with regard to certified checks. While the Certified Checks control account is kept by the general bookkeepers, the account itself is kept by the check desk. As certified checks are received

they are checked off the certification sheets. Certifications which are outstanding for a considerable period are entered from the certification sheets in the certified check ledger. The balance of the ledger and the sheets are proved each week with the control account of the general bookkeepers.

### **Check Desk Proof**

For the purpose of showing a summary of its operations and furnishing control figures for the general books, the check desk prepares a daily proof of its operations (Form 84). The credit side of the proof shows the credits to the various tellers and departments of the bank for items which they have sent. Items which come from the clearing house, it will be recalled, are credited to the paying teller. To offset these credits the debit side of the proof shows the disposition which the check clerk has made of the items received. Disposition has been made by sending foreign items to the foreign ledgers, domestic items to the domestic ledgers, rejects to the city collection department, certified checks to the certified check ledger, and general account items, such as cashiers' checks, to the general bookkeepers. Accordingly, charges are made to each of these for the amount sent them.

### **Work of Domestic Bookkeepers**

The stage in the accounting work of the bank has now been reached where all the original entry material has been sorted according to ledgers, either by the operating departments, the ticket journal department, or by the check desk, control figures have been sent to the general bookkeepers, and the material is ready to be posted. This work for the domestic accounts of the bank is performed by the domestic bookkeepers.

The work of the bookkeeping force consists of two main operations: (1) posting to the depositors' accounts, and (2)





preparing statements of accounts to be sent to customers. As will be shown presently, these two operations are performed concurrently, the one acting as a check upon the other. In accordance with this scheme the bookkeeping force is divided into small units each one of which keeps the records required for the accounts of a single ledger volume. Each of these unit forces consists of a ledger bookkeeper and a statement clerk.

### Ledger Classification

The importance of the classification of the ledgers containing depositors' accounts has already been indicated. Each department in the bank uses this classification as a basis for charging and crediting the items contained in its daily proof. Specifically the scheme of classification depends upon the information which the bank under consideration wishes to obtain from its ledgers.

The bank upon the practices of which this study is based, for example, measures its domestic business in terms of states and classes of accounts. Accordingly, to facilitate the work of obtaining statistics of the business transacted the accounts are arranged by states and by kinds: individual accounts, national bank accounts, state bank, trust companies, and savings bank accounts. In the given ledger the accounts are arranged alphabetically, the individuals by surnames and the banks by cities.<sup>1</sup>

<sup>1</sup> At the time of writing, the ledger classification is as follows:

#### INDIVIDUAL ACCOUNTS

##### Ledger

- 1 Alabama, Arizona, Arkansas, California, Colorado, Connecticut, Delaware, District of Columbia, Florida, Georgia, and Idaho
- 2 Illinois, Indiana, Iowa, Kansas, Kentucky, and Louisiana
- 3 Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, and Missouri
- 4 Montana, Nebraska, Nevada, New Hampshire, New Jersey, New Mexico, North Carolina, North Dakota, and Ohio
- 5 Oklahoma, Oregon, and Pennsylvania
- 6 Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin, and Wyoming
- 7 New York—A
- 8 " " —B
- 9 " " —C

### Ledger System

The form of ledger used by the bank is the Boston ledger illustrated in Form 85—a record which is well adapted to conditions where it is desired to show changes taking place each day in an account. This ledger is made up in bound form with a sufficient number of pages to suffice for a period of six months. In the center of each page the names of the customers are entered in alphabetical order, one to a horizontal line, sufficient blank space being provided for the addition of new names in alphabetical order during the period in which the ledger is in use. Each page is ruled vertically into columns, one for each day's entries. The whole page contains six of these columns, enough for one week's work. The column for each day's entries is further divided into two columns, the left one being for the entry of all debits to the account for the day, and the right for the credits and for the pencil balance.

#### INDIVIDUAL ACCOUNTS (Continued)

- |    |              |
|----|--------------|
| 10 | New York—D—F |
| 11 | " " —G—I     |
| 12 | " " —J—L     |
| 13 | " " —M—N     |
| 14 | " " —O—R     |
| 15 | " " —S       |
| 16 | " " —T—Z     |

#### NATIONAL BANKS

- |    |   |
|----|---|
| 17 | Alabama, Arizona, Arkansas, California (including Hawaii), Colorado, Connecticut, Delaware, District of Columbia, Florida, Georgia, and Idaho |
| 18 | Illinois, Indiana, Iowa, and Kansas   |
| 19 | Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, and Mississippi   |
| 20 | Missouri, Montana, Nebraska, Nevada, New Hampshire, New Jersey, New Mexico, and New York  |
| 21 | North Carolina, North Dakota, Ohio, and Oklahoma  |
| 22 | Oregon, Pennsylvania, Rhode Island, South Carolina, South Dakota, and Tennessee   |
| 23 | Texas, Utah, Vermont, Virginia, Washington (including Alaska), West Virginia, Wisconsin, and Wyoming  |

#### STATE BANKS, TRUSTS, AND SAVINGS BANKS

- |    |   |
|----|---|
| 24 | Alabama, Arizona, Arkansas, California (including Hawaii), Colorado, Connecticut, Delaware, District of Columbia, Florida, Georgia, Idaho, and Illinois |
| 25 | Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, and Mississippi  |
| 26 | Missouri, Montana, Nebraska, Nevada, New Hampshire, New Jersey, New Mexico, and New York  |
| 27 | North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, and South Dakota                                      |
| 28 | Tennessee, Texas, Utah, Vermont, Virginia, Washington (including Alaska), West Virginia, Wisconsin, and Wyoming   |

[illegible]

Form 85. Customers Ledger. (Size 19 x 12.)

### Routine Work of Bookkeeper

The work of the ledger bookkeeper for a given day properly begins in the early part of the afternoon and terminates late the next morning. Clearness will therefore be served best by following the work of the operating rather than the calendar day.

When the ledger has been prepared for the day's postings, only the credit balances will appear in the column for the given day. The first items coming to the attention of the bookkeeper are the cash letters from the mail teller's department. These letter credits have been sent to the ledger by the mail tellers during the morning, as was observed in the discussion of the receiving operations of the bank. The bookkeeper enters the amounts of the letters to the credit of the proper ledger accounts and takes a record of each posting on a proof sheet for future use in checking his work against that of the mail department. The letters are then returned to the mail tellers for acknowledgment and the duplicate of the acknowledgment comes to the statement clerks to be used in posting their sheets.

The next items to come to the attention of the bookkeeper are the checks sorted and charged to him through the morning work of the check desk. These have already been sorted and listed according to accounts by the check desk. The checks are not posted separately, merely the totals for each account are entered according to the accompanying lists. The checks are then passed to the statement clerks who post each one separately, thereby aiding in proving the accuracy of the ledger. In the case of accounts having a large number of checks for any one day the work of posting each individual check becomes prohibitive. Accordingly the statement clerks post one amount and file a list of the checks included in the charge to be returned to the customer with the statement.

Throughout the entire afternoon both debit and credit

tickets from the ticket journal department and single credit tickets from the note teller's, city collection, discount, loan, bond, country collection, and the foreign teller's department, deposit tickets from the receiving teller, and checks from the afternoon work of the check desk are received and posted by the bookkeeper. Bookkeepers in charge of the accounts of correspondent banks also receive for posting to the debit of the accounts kept by them tickets from the collection ledger covering collections sent out on a transfer basis and for which the proper time of transfer has elapsed, as well as duplicate letters of transmittal from the transit department covering items sent out for collection on a charge basis. Later in the afternoon the afternoon mail from the mail tellers, exchange tickets charging various accounts for exchange on checks collected by the transit department, and the certification sheets authorizing the charging of certified checks against the various accounts, are received by the bookkeeper. For the totals of each of these classes of items a proper entry is made to the debit or credit of the customer's account.

To facilitate checking his work the bookkeeper indicates the source of each item posted to his ledger by using different colored inks. Thus the credits from the morning mail and the morning debit items from the check desk are entered in purple ink, the various tickets and the afternoon exchanges, certifications, etc., in black ink, and the entries constituting the credits to the account of a customer from the afternoon mail, in green ink. Through the use of this color system it is possible for the bookkeeper to locate readily the source of any entry should a question concerning it arise later.

When the entries for the day have been completed the bookkeeper carries forward the new credit balance of each account for the following day. This is done by adding the credits made during the day to the previous day's balance and deducting the debits.

### Ledger Proof

A very complete system of checking and proving the accuracy of the ledgers is used by the bank. In the first place each bookkeeper proves the accuracy of his total balances. For this a special form is used upon which the total of the various entries made the preceding day is recorded. The operation of this proof is as follows: To the total of the balance of the accounts in his ledger for the preceding day the bookkeeper adds the sum of the credits for the given day, as reported by the operating departments. From the gross credit obtained in this manner is deducted the sum of the debits sent to his ledger for the given day, as reported by the operating departments. The amount thus obtained should agree with the total balances shown by the accounts in the ledger.

### Statement of Account

The proof just described does no more than prove that the total of the balance in the ledger is correct. It does not provide a check over the accuracy of the balance of each account in the ledger. This check is provided by the work of the statement clerks. It is the custom of the bank to render the depositor a statement of account at the close of each month—or more often if he requests it—showing the amounts credited to the account, the drawings made, and the latest balance. Along with the statement the bank sends the customer the paid vouchers, checks, notes, etc., which have been charged to his account. The customer is expected to compare this statement with his records and to report the result to the bank whether his figures agree with the bank's or not. This process provides a check upon the work of the bookkeeper from an outside source.

The method of preparing the statement is also a check upon the bookkeeper's work. As has already been indicated, the preparation of statements for the accounts in a given ledger

parallels the posting. So far as it is practicable the statement clerks make their postings from different material than do the bookkeepers. Thus debits from the check desk are entered on the statement sheets from the items themselves, the details of each case being given, while the bookkeepers enter only the totals from the lists furnished by the check desk. The statement clerks post mail credits from the duplicate letters of acknowledgment prepared by the mail teller's department, while the bookkeepers post these credits from the incoming remittance letters direct. The receiving teller's credits are posted to the statement from duplicate credit sheets prepared in the receiving teller's department, while in the ledgers posting is made from the deposit slips themselves. At the close of the day the statement clerks and the bookkeepers compare their balances on each account and rectify any errors which may have been made.

The third check upon the accuracy of the ledgers is the control accounts of the general bookkeepers' department. When each individual account has been proved against the statement clerks' records and the proof of the ledger has been prepared, a statement showing the total of the balances in each ledger is sent to the general bookkeepers' department. In the meantime the general bookkeepers have built up control accounts over each ledger from the proofs sent them by the operating departments of the bank, the check desk, and the ticket journal department. The general bookkeepers check the balances furnished them by the customers' bookkeepers with their own figures and bring any errors discovered to the attention of the latter.

### **Disposition of Entry Material**

When the proof for the day has been verified all tickets and checks which were used as a basis for the entries made the previous day are filed. The debit and credit tickets are



filed by numbers for future reference, deposit tickets are sent back to the receiving teller for filing, and all checks, notes, and similar items are placed in the check and statement files whence they are sent to the customer at the time that the statement is forwarded to him. Before sending the statement, however, the canceled vouchers are carefully checked against it to insure the accuracy of the enclosure

### **"Holds"**

In addition to the regular original entry material the bookkeepers frequently have to deal with "holds" A hold may be defined as a temporary debit entry made to an account pending the arrival in the bookkeepers' department of authority to make the debit permanent In studying the work of the operating departments it has already been noted that the hold is the common method used by a department to make sure that a customer's account will not be overdrawn by a debit which is to be made When he receives a request to hold an amount the bookkeeper makes a debit entry in pencil with a notation as to what department sent the request. Later, on the same day usually, the bookkeeper receives a ticket or some other debit item covering the hold, at which time he makes a permanent entry charging the account. If for any reason a debit covering the hold should not be sent to the bookkeeper within twenty-four hours, he withdraws it and is relieved of responsibility should an overdraft occur. It should be said, of course, that the hold does not affect the depositor's balance except for the purpose of meeting drawings which may be made while it is in effect.

### **Time Deposits**

For the purpose of securing higher interest rates on funds which are not needed in the immediate future, customers frequently place these funds in a special time deposit account.

These accounts are kept in separate ledgers, and since by nature such accounts are very inactive the ledgers are kept by a member of the bookkeeping force who is also in charge of a ledger containing demand deposit accounts. One sheet of a ledger is devoted to a customer's account.

In order that the bank may avail itself of the provision of the law which permits it to maintain a reserve of only 3 per cent against time deposits, these deposits are made with the understanding that they can be withdrawn only after a 30-day notice of intention to withdraw has been filed with the bank. When a customer who has a time deposit account wishes to make a withdrawal he files a notice in accordance with this provision. Upon receipt of this notice the customer's time deposit account is charged and an account known as "Time Deposits—Notice of Withdrawals Given," is credited. The withdrawal itself, when made, is charged to this account. The "Time Deposits—Notice of Withdrawals Given" therefore represents deposits against which reserve at the rate for demand deposits must be kept, but they are not payable until the notification period has expired.

Time certificates of deposit are similar in nature to time deposits, although the accounting for them is done by the general bookkeepers. These certificates are recorded in a tickler ledger according to due dates. To meet reserve requirements, 31 days before its due date the amount of each certificate is transferred from the Time Certificate of Deposit account to the Demand Deposit account. When the certificate is presented for payment it is charged to Demand Deposits just as are cashier's checks and similar instruments.

### Inactive Accounts

Occasionally a depositor's account will show no change for a considerable period of time. In order that the bookkeeper may not be burdened with the unnecessary labor of

forwarding unchanged balances each day, such an account as this is transferred to an inactive ledger. This book is an ordinary two-column ledger showing on the credit side the amount and date of the transfer and on the debit side the final disposition of the balance. At intervals the inactive ledger is examined and an effort is made to ascertain the reason for the inactivity of the account. Frequently the balances are very small ones representing differences between the bank's records and those of customers who have withdrawn their accounts. In such cases, the matter is brought to the attention of the customer and the amount is usually withdrawn. On the other hand, should an additional deposit be received from a depositor whose account appears in the inactive ledger, or some other sign of activity be shown, the account is transferred back into the regular deposit ledger.

### **Statistical Work of Bookkeepers**

The bookkeepers also have the duty of supplying certain information of a statistical nature to the officers and others of the bank. Whenever an account of the bank is closed and the balance withdrawn, they notify all departments which are particularly interested, such as analysis, credit, and signature control. Each day the bookkeepers prepare for the use of the officers a report containing a list of all accounts having a balance of more than \$500,000 and \$1,000,000 respectively, and of all those which have shown a change in balance during the day of \$100,000 or more in either direction.

### **Passing upon Checks Before Payment**

In the discussion of the work of the departments which receive checks drawn upon the bank itself, it has been said that the bookkeepers act as a court of final resort in deciding upon whether or not the bank will honor an item presented for payment. Specifically this work consists in:

1. Caring for stop-payment orders
2. Watching for overdrafts
3. Verifying signatures
4. Examining items for filling, date, indorsement, etc.

The work of caring for stop-payment orders and watching for overdrafts is performed by the ledger bookkeepers themselves, while signatures are verified and items are examined for filling by a closely related department known as the signature control department

*Stop-Payment Orders.* Stop-payment orders come to the attention of a stop-order clerk. Usually the orders are in writing, but they may be given verbally. In the latter case, however, the bank asks the sender to confirm the order in writing. If the order pertains to a check recently issued search is made through the check and statement files and also on the customer's statement in process of preparation to determine whether the item has been paid since the last statement was rendered. If payment has already been made the customer receives an advice of the fact and the bank, of course, can do nothing in the matter. If, on the other hand, payment has not been made the advice is sent to the customer acknowledging receipt of the order and promising to see that it is carried out. This advice states that it is assumed that the customer has examined his records and determined that the check has not already been returned to him paid.

A list of all stop-payment orders received is sent to the paying teller, to the certification department, and to the bookkeeper in charge of the ledger containing the account of the drawer of the item. Each bookkeeper keeps a stop-payment card upon which he enters the number of the check, the date the check was issued, and the amount. The card is filed in a stop-payment file and it becomes the duty of the bookkeeper to watch carefully all checks received by him and avoid entering in the ledger those against which stop-orders are in effect.

*Overdrafts.* As he posts, the bookkeeper notes whether the customer's balance is adequate to take care of the debit items and when an account is overdrawn he reports the fact upon an overdraft slip to the officer in charge of the depositor's territory. Knowing the nature of the customer's account the officer is in a position to decide whether or not the overdraft is to be carried. Due to the fact that the bank has such a large volume of out-of-town business many of these overdrafts are caused by checks being drawn against funds delayed in transit and are of comparatively little consequence, hence the officer promptly approves and signs the slip as authority to the bookkeeper to carry the overdraft. In other cases, however, there is doubt as to the advisability of carrying the overdraft. In instances of this sort it is the usual practice to send the overdraft slip to each operating department which handles credits to depositors' accounts. In these departments search is made through the work in process and on the overdraft slip is indicated whether or not the department has funds for the depositor which have not yet been posted. The overdraft slip then returns to the officer who approves or rejects the transaction. Then it is sent to the credit department where it is filed in the credit folder of the customer.

*Signatures.* The function of verifying signatures for the whole bank is performed by the signature control department which maintains an up-to-date file of the signatures with which the bank comes into contact. Accordingly all checks coming to the check desk are scrutinized by this department before they are passed to the bookkeepers for posting. From long acquaintance with the signatures of the bank's clients the members of the signature department become familiar with the majority of them and can quickly and accurately examine an astonishingly large number of items in a day. When a signature is not known it can be quickly verified by reference to the card file kept by the department. As a matter of

convenience the signature control department also scrutinizes the items with regard to proper dating and filling

At the time a customer opens an account the bank requires him to prepare signature cards for its future use. Different forms of cards are used for banks, for individuals, and for other business concerns. Upon these cards are given the signatures of those authorized to sign, the signatory powers enjoyed by each signer, the individuals required to sign each instrument, etc. In case the customer is a corporation the bank authenticates the signature card by obtaining a certified copy of the resolutions of the board of directors of the corporation authorizing officers and others to sign. On the reverse side of the signature card for individual customers such information as name of person introducing the subject to the bank, business of subject, address, and date of opening the account is entered. Excepting in the case of correspondent banks, duplicate signature cards are filled out for each depositor, and the second set is kept by the paying teller to assist him in verifying signatures for the payment of checks.

*Irregular Items* In a large bank the function of protecting itself against paying unauthorized checks drawn against the accounts of bankrupts, deceased persons, concerns in the hands of receivers, accounts which have been attached, etc., becomes important. The matter of passing upon the authority of those who seek to draw checks against balances of this sort rests with the legal department which obtains and files copies of court orders, wills, etc., and consults them before approving payment. To prevent passing items of this sort without referring them to the legal department the bookkeepers place a stamp of distinctive shape opposite the name of each account which cannot be drawn against in the regular way.

In general, the procedure in dealing with a check which is seriously irregular in signature, indorsement, filling, insufficient balance, or against which a stop-payment order is in

effect, is for the check desk department to charge and send it immediately to the city collection department, together with a slip showing reasons for refusing payment. This latter department communicates with the last indorser and obtains reimbursement. The bank, however, attempts in every way consistent with good banking to spare its customers the inconveniences which come from having items returned. In returning a check drawn by an out-of-town depositor because of insufficient funds, for example, the bank includes in its notice an opinion that the overdraft is caused by funds being delayed in transit and it requests the holder to present the item for payment again shortly instead of returning it to the maker. In the case of a comparatively small irregular check drawn in favor of a concern of high credit rating, the bank sometimes makes the payment and communicates with the drawer of the item by letter. The understanding is, of course, that the payee of the item whose indorsement appears thereon will make it good in case the maker refuses payment.

### Interest on Deposits

As a special inducement for customers—both banks and individuals—to maintain balances of considerable proportions and in order to meet the competition of other banks, the bank at times pays interest upon deposit balances. As a basis for calculating interest to be paid depositors the bookkeepers prepare each morning a list of interest balances which they enter on interest sheets of which there is one for each depositor. The interest balance for a particular account is obtained as follows. To the credit balance for the preceding day are added any deposits credited to the customer's account which are available for use by the bank on the current day. From this sum are subtracted all debits made to the depositor's account during the day. The result is the interest balance.

It will be noted that the interest balance is less than the

actual balance by the amount of all items credited to the depositor's account during the current day, excepting those which the bank can use in its loaning operations. The reason for this is that the bank generally gives the customer credit for items before it has the use of them. All credits therefore appear in the actual balance. The interest balance for a given day, however, represents in so far as is practicable only those funds deposited by the customer of which the bank has full use. Uncollected funds therefore are excluded from the interest balance.

The reason for making a deduction for uncollected funds in arriving at the interest balance may be illustrated by means of a concrete example. Suppose a customer deposits in the National City Bank of New York on January 2, a check for \$5,000 drawn upon a clearing house bank. The National City Bank would give him immediate credit for \$5,000 in his deposit account, thereby increasing his actual balance for January 2 by this amount. The bank, however, cannot collect the check until the ten o'clock session of the clearing house on January 3. In other words, the bank does not have the use of the check for loaning purposes during the day of January 2 at all. This amount is therefore properly deducted from the actual balance in arriving at the amount upon which the bank should pay interest for January 2.

The practice of eliminating uncollected credits from a depositor's account for one day takes care of the time required for the bank to collect sights, trusts, clearing house items, etc., in fact all cash items save countries. In case the bank has charged the customer exchange on a country item, it figures that the amount of exchange collected reimburses it for loss of interest and it therefore makes no deduction for an item of this sort. On country items drawn payable at a discretionary point, however, no exchange is charged and such uncollected items are therefore deducted in arriving at the interest



balance To care for these "interest delays," as they are termed, the transit department inspects the incoming cash mail and indicates on the letters the amounts to be delayed and the time required for collection. For country items taken in by the receiving teller the transit department sends the bookkeepers a monthly list of the interest delays for each depositor. All these interest delays are entered in a separate column on the interest sheets and at the end of the month they are combined for each account and the proper deduction is made in calculating the interest.

The following table shows a comparison of an interest balance with an actual balance for a given day

	Interest Balance	Actual Balance
Actual balance as shown by ledger at beginning of day . . . . .	\$ 75,000	\$ 75,000
Deposited today		
Proceeds from discounts, loans, and other immediately available items	25,000	25,000
Clearing house checks, country checks with exchange trusts, etc., arriving too late to be collected today		10,000
Country checks (discretionary, 3 days)	...	5,000
	<hr/> \$100,000	<hr/> \$115,000
Less checks paid	20,000	20,000
	<hr/> \$ 80,000	<hr/> \$ 95,000
Less interest delay \$5,000 at 2 days	10,000	
	<hr/> \$ 70,000	<hr/> \$ 95,000
Balance forwarded to next day's work	<u>\$ 95,000</u>	<u>\$ 95,000</u>

### Interest Department

When the interest sheets for the given day are completed they are passed to the interest department, which performs

the work of calculating and accounting for interest paid on balances. The clerks from the interest department compare the interest sheets with the ledger balances of the bookkeepers to ascertain their accuracy and post the interest balances to the interest ledger. The function of this ledger is to record the interest balance of each interest-bearing account. Each customer who receives interest has a separate vertical column for entry of his daily interest balance. All interest balances for a given day are entered on the same line, so that at the end of the interest month by adding the ledger columns from top to bottom the sum of the balances maintained by each customer may be obtained, while by adding the lines from left to right the total amount bearing interest each day is obtained.

On the twenty-sixth day of each month the interest clerks calculate the interest due each customer. This is done by computing interest for 30 days upon the average balance shown on the interest sheet. The interest department also attends to settling with the customer for interest allowed him. Usually the customer wishes his account to be credited for the amount. In this case the interest department enters the amount on posting sheets which are sent to the ledger bookkeepers for credit to the customer's account. If the depositor desires to receive a cashier's check for the interest due him, the accounting department sends him the check. In any event the interest sheet prepared by the bookkeeper is sent to the customer as evidence of the allowance.

### Accounting for Interest

The interest allowed depositors each month is charged to the Interest Paid account and credited generally to the depositors' accounts or to Cashier's Check account. In some cases, however, the agreement in effect between the bank and the recipient of interest provides for payment at other periods

than the close of the month. In such cases credit is made to the Reserve for Interest—Domestic Bookkeeping Department account at the end of the month. When payment is made the amount is charged to this account. The Interest Allowed on Deposits account is therefore an expense account representing the total amount of interest on depositors' balances paid by the bank. This is divided into sections, for statistical purposes, according to classes of accounts—individuals, banks, and time deposits. The Reserve for Interest account is a liability account showing amounts accrued and unpaid.

### Analysis of Depositors' Accounts

Frequently it is desirable to know the relative profitableness of a customer's account to the bank. When a question of this sort arises it is referred to a department known as the analysis department, whose function it is to determine the cost and the profit or loss resulting from carrying customers' accounts and to submit their results in the form of reports, as illustrated in Form 86.

In analyzing an account the base of the calculation is the average loanable balance. This consists of the average of the daily ledger balances of the account less amounts not available to the bank for loaning purposes, i.e., the reserve maintained against the deposit and uncollected funds contained in the balance. In other words it is the interest balance, less reserve maintained. This figure is computed for each month contained in the period covered by the analysis.

From the average loanable balance the gross income from the account is computed. The rate of gross income is the average rate obtained by the bank on all of its investments for the month under consideration. Interest on the average loanable balance at this rate for one month gives the gross income from the account.

In deriving the net income produced by an account from



the gross income, two deductions are to be made—the interest paid the depositor, and the cost of maintaining the account. No difficulty is encountered in obtaining the interest paid figure, since it is the amount computed by the interest department and paid the depositor.

The expense of maintaining an account consists of three parts: the direct expense, the special service, and the overhead expense. Direct expense is that incurred through handling items for the customer in the operating departments of the bank. Knowing the total expense of carrying on a given operation in a department for one month, the analysis department arrives at a monthly average unit cost for each item passing through that process, by dividing the total cost by the number of items handled. This unit figure is then multiplied by the number of items handled for the account to be analyzed in order to determine the cost of furnishing the particular service for the account. The same analysis is made of each operating service used by the depositor, and the total of all these costs gives the direct expense of maintaining the account.

Special service expense is that incurred through furnishing such services as giving information on foreign trade, industrial service, etc. Since the service departments do not handle specific items, this expense cannot be reduced to an item basis. The cost of this service is therefore distributed on an estimated basis among the customers using it.

The indirect or overhead expenses are such as general and administrative expense and others which cannot be directly allocated to depositors' accounts. If the bank cares to take cognizance of these costs they may be distributed on some arbitrary basis. Such a figure is, however, at best unreliable and it is considered good practice to disregard these expenses entirely in the analysis figures.

It is apparent that the system of analysis just outlined does not produce an absolutely accurate figure for profits.

The system, however, must be appraised in the light of what information is really wanted by the bank. A bank is not particularly interested in knowing the exact profit obtained from an account, at least not enough so to incur the outlay which would be necessary to maintain such a system of analysis were it possible to arrive at an accurate figure. The bank expects an analysis to show three things: (1) whether carrying the account produces regularly a profit or a loss, (2) whether the bank is furnishing service to the depositor in excess of what the profitableness of the account calls for, and (3) whether the depositor habitually draws against uncollected funds. All things being taken into consideration the system just outlined meets the requirements of a bank in an economical way.

## CHAPTER XXII

### FOREIGN BOOKS

#### Divisions of Foreign Accounts

The foreign accounting of the bank is divided into two parts. (1) the accounting for balances maintained by the bank with foreign correspondents, and (2) the accounting for balances kept on deposit in the bank by foreign correspondents. Mention has already been made of the fact that the account relations between the bank and its foreign correspondents may consist of dollar deposit accounts kept in the American bank by the foreign correspondent, or they may consist of foreign currency deposit accounts kept with the foreign correspondent by the American bank. The former class of accounts is spoken of as the "their," or "due to foreign banks" accounts, while the latter is spoken of as the "our," or the "due from foreign banks" accounts. The "due to" accounts are liabilities of the bank, while the "due from" accounts are assets. It is understood, of course, that foreign non-banking concerns and individuals have only "due to" accounts with the bank, just as do its domestic customers.

From this classification of the foreign bank accounts it must not be thought that the foreign correspondent banks themselves are always of two classes—those which maintain deposit balances with the American bank, and those with which the bank maintains deposit balances. The American bank does keep accounts with some foreign banks which do not keep accounts with it, it is true, and the American bank also holds balances to the credit of some foreign banks with which it does not keep a balance. With each of its larger correspondents, on the other hand, the American bank has

reciprocal accounts, i.e., there is both an "our" account and a "their" account relation. For bookkeeping purposes, however, these two accounts with the same bank are kept as far separated as though the bank were accounting with separate institutions.

### Foreign "Their" Accounts

The "due from foreign banks" accounts, which are kept for the purpose of trading in foreign exchange, have already been described in the work of the traders. The "due to foreign banks" accounts, which are the foreign counterpart of the domestic customers' accounts, are kept by the foreign bookkeepers' department. The work of this department is similar to that of the domestic bookkeepers' department in most respects, hence certain important differences which arise from the peculiarities of international banking procedure will receive the main emphasis in the following discussion.

### Foreign Drafts

The foreign draft differs from the domestic check in that it is generally drawn in duplicate and in that the drawer usually advises the bank that he has drawn it. The arrangement is generally that whichever of these items arrives in the bank first—advice, original, duplicate, or triplicate copy of the draft—serves as authority to charge the account of the drawer. As a result a depositor's account may be charged from the original draft itself, as in the domestic work, or it may be charged from the advice or from the duplicate. Hence in foreign bookkeeping an important problem is that of making sure that each drawing is honored only once.

### Drafts Section

For the purpose of handling these drafts and advices which are to be charged to foreign customers' accounts, a special



drafts section is maintained in the foreign bookkeeping department. There is a subsection for each foreign ledger. The drafts section performs in general the work of the check desk in the domestic division of the bank, in that it prepares the drafts for posting. The term "drafts," however, includes not only original drafts, but duplicates and advices as well.

In the large majority of cases the drawers of foreign drafts advise the bank of their drawings, and these advices constitute authority to charge their accounts. An advice usually reaches the bookkeeping department before the corresponding draft does, since the drawer sends the advice direct to the bank while he sends the draft to the payee, who presents it to the bank for payment in a more or less roundabout manner. In the typical procedure, therefore, the account is debited upon receipt of the advice and the draft is paid by the bank subsequently. The advice comes to the proper drafts clerk direct from the incoming mail department. The drafts subsections deal with the corresponding ledgers by means of debit tickets exclusively. After it has been ascertained that the signature appearing on the advice is authentic and that the advice is regular in every respect, it is recorded in the drafts book of the subsection. Thereupon a debit ticket charging the account of the drawer is drawn. This ticket passes through the ticket journal department for entry to the control accounts whence it is sent to the proper ledger.

#### **Customers' Drafts Advised and Outstanding Account**

While the account of the sender of the advice has been charged, the bank has not reduced its liability. The draft to which the advice applies is still outstanding and will have to be paid when it is presented. To offset the charge which has been made, a credit is made to an account entitled "Customers' Drafts Advised and Outstanding," for the total amount of all debit tickets which have been drawn by the

**draft clerk** An entry of this sort, in effect, segregates funds out of foreign depositors' accounts for the purpose of meeting drafts which they have drawn. The Customers' Drafts Advised and Outstanding account is thus in a way similar to the Certified Check account in that it represents funds which have been segregated to pay instruments already charged to the accounts of the drawers. In the case of certified checks, however, the bank is obliged to pay the check when presented, while in charging an advice to a customer's account the bank assumes no obligation to pay the draft when presented if the balance in the account is not sufficient at the time of presentation or if the draft itself is not correctly drawn. Since the drafts are payable when presented this account has the same status as a demand deposit. It is accordingly kept in one of the foreign ledgers as an ordinary deposit account.

There is one Customers' Drafts Advised and Outstanding account for each ledger. For convenience the Customers' Drafts Advised and Outstanding accounts for all the foreign individual ledgers are cared for in the S-Z foreign individual ledger, while the same accounts for all the foreign bank ledgers are contained in the O-Z foreign bank ledger. The tickets debiting drawers' accounts are sent to the various ledgers from the ticket journal department and the tickets crediting the Customers' Advised and Outstanding account are sent to the two ledgers containing these accounts. So far as the proof of the ticket journal department is concerned, entries made to the Customers' Drafts Advised and Outstanding account are indistinguishable from the ordinary cross-credit transactions, debiting one set of customers and crediting another.

### **Incoming Drafts**

When a draft which has been advised in this manner is presented and paid it is charged to the Customers' Drafts

Advised and Outstanding account instead of to the account of the drawer.

Foreign drafts come to the check desk through the usual channels. Since at the check desk there is no way of knowing which items will be returned unpaid by the foreign bookkeepers, the whole amount of drafts is charged in bulk to the latter department. The drafts are examined by the drafts clerks and those which cannot be paid are returned to the check desk. A report is then sent to the check desk showing the distribution of the drafts approved for payment to the two ledgers containing the Customers' Drafts Advised and Outstanding accounts. This report is incorporated in the daily proof of the check desk department whereby it serves the function of giving the general bookkeeper control figures over these charges. The debit entries to the Customers' Drafts Advised and Outstanding accounts contained in the O-Z bank and the S-Z individual ledgers are made from tickets which pass directly from the drafts clerk to the ledger bookkeepers without passing through the ticket journal department proof. By this arrangement a double charge to the general accounts is avoided.

### Payment of Drafts

Many foreign customers—individuals for example—do not as a general rule advise the bank of their drawings. It also frequently happens that foreign drafts are presented to the bank for payment before the corresponding advice arrives. In cases of this sort the bank honors the drafts, unless it has standing instructions from the drawers not to do so. When the bank pays the draft of a customer before it receives an advice and the customer is one who regularly sends advices of drawings, it informs him of its action and requests him to send a confirmation. In handling an item of this sort, for uniformity's sake, the same entry is made as for an advice,

that is, the transaction is passed through the Customers' Drafts Advised and Outstanding account. Care is taken to see that the advice, if any, is not charged to the customer's account when it is received subsequently.

The foregoing represents the method used in handling foreign drafts received through the clearings and also from most of the operating departments of the bank. Drafts presented to the paying teller or the certification department are handled somewhat differently, however, in that they are not paid or certified until the drafts clerk has examined them. If payment is in order the drafts clerk has a "hold" placed against the account for the amount of the draft and returns it together with his authorization stamp to the paying teller or certification department for action. The entry debiting the account of the drawer and crediting the Customers' Drafts Advised and Outstanding account is made at this time rather than when the draft has returned from the check desk.

### **Drafts Book**

For the purpose of maintaining a permanent record of all drafts paid by the department each drafts clerk keeps a drafts book. In this book there is a separate section for each depositor in which each draft and advice coming to the bank is entered. This entry when completed includes the name of the customer, the date of arrival of the draft, the date of advice, which is the date upon which the instrument was drawn, the number of the draft, the amount, the date paid, and any remarks in regard to the instrument, such as the fact that an additional copy has been received, etc.

The chief function of the drafts book is to enable the bank to avoid honoring an item and charging it to the drawer's account more than once. Before either a draft or an advice is acted upon the drafts book is examined. This examination indicates whether a charge is to be made to the account of

the drawer at this time, and whether payment is to be made if the item presented is a draft or a duplicate. The total of the items remaining unpaid according to the "Date Paid" column of the drafts book represents the balance of Customers' Drafts Advised and Outstanding account for the corresponding ledger, and proof is made between this book and the account each week.

### Ledger Bookkeepers

With the exception of the drafts, the material for posting to the foreign ledgers passes through the same process as the material for the domestic ledgers. Double tickets pass through the ticket journal department, single tickets through departmental credit journals, and cash letters and deposit tickets come directly to the foreign bookkeepers after control figures for the general books have been prepared.

The foreign bookkeeping force is organized by ledger volumes.<sup>1</sup> Each ledger force consists of a ledger bookkeeper

<sup>1</sup> The ledger volumes are arranged as follows:

FOREIGN BANKS		
1 A to C	3 G to H	5 O to Z
Argentina	Germany	Panama
Australia	Great Britain	Paraguay
Austria	Greece	Persia
Azores	Guatemala	Peru
Belgium	Haiti	Philippine Islands
Bermuda	Hawaii	Poland-Porto Rico
Bolivia	Holland	Portugal
Brazil	Honduras	Roumania
Bulgaria		Russia
Canada	4 I to N	Salvador
Canary Islands	Iceland	Serbia
Chile	India	Spain
China	Italy	Sweden
Colombia	Jamaica	Switzerland
Costa Rica	Japan	Trinidad
Cuba	Java	Turkey in Asia
Czecho Slovakia	Jugo Slavia	Turkey in Europe
	Liberia	Uruguay
2 D to F	Lithuania	United States
Denmark	Luxembourg	Venezuela
Dominican Republic	Madeira	Virgin Islands
Dutch Guiana	Mexico	West Coast Africa
Dutch West Indies	Nicaragua	
East Africa	Norway	
Ecuador		
Egypt		
Finland		
France		

and an accounts current, or statement, clerk, and these two act as a check upon each other just as do the ledger bookkeepers and statement clerks in the domestic bookkeeping department. Entries in the foreign ledgers from different sources are posted in ink of different colors, just as are those in domestic ledgers. The great bulk of the original entry material consists of tickets, in contrast to the large number of checks contained in the material for the domestic book, but these tickets are posted in the same way as those for the domestic ledgers. Holds are far more prevalent in the work of the foreign section but they are not handled in a distinctive way.

### Overdrafts in Foreign Accounts

Overdrafts occur with greater frequency in foreign accounts than in domestic. From the standpoint of the officers to whom overdrafts are referred, the accounts may be divided on the basis of overdrafts into three classes:

- 1 Those which have no overdraft privileges
- 2 Those enjoying the privilege, by virtue of prearranged

INDIVIDUAL ACCOUNTS		
6 A to C	8 I to G	12 Q to R
Argentina	Finland	Roumania
Australia	France	Russia
Austria	Germany	
Azores	Great Britain	13 S to Z
Belgium	Greece	Salvador
Bermuda	Guatemala	Serbia
Bolivia		Spain
Brazil	9 H to L	Sweden
Bulgaria	Haiti	Switzerland
Canada	Hawaii	Trinidad
Canary Islands	Holland	Turkey in Asia
Chile	Honduras	Turkey in Europe
China		Uruguay
7 C to E	10 M	United States
Colombia	Madagascar	Venezuela
Costa Rica	Mexico	Virgin Islands
Cuba		West Coast of Africa
Czechoslovakia	11 N to P	Due to Branches
Denmark	Nicaragua	Due to Governments
Dominican Republic	Norway	Account
Dutch Guiana	Panama	Foreign Time Deposits
Dutch West Indies	Paraguay	
East Africa	Persia	
Ecuador	Peru	
Egypt	Philippine Islands	
	Poland	
	Porto Rico	

terms, of overdrawn their accounts up to a certain amount

### 3 Reimbursement accounts

The first-named class of accounts corresponds to the domestic accounts in that the bank undertakes to pay the customer's drafts only when he has sufficient funds on deposit to meet them. If an account of this sort shows an overdraft the usual search for prospective credits is made through the operating departments, and if no funds are found the officer of the bank to whom the transaction is referred generally refuses to honor the proposed drawing.

Foreign banks engaging actively in foreign exchange transactions find it both convenient and profitable to overdraw their accounts at times. To enable themselves to do this they make arrangements with their correspondents to honor overdrafts against their accounts up to certain amounts. By custom the correspondent receives a high rate of interest upon overdrafts, not only from banks but from all other foreign accounts as well. Many of the banks having this privilege, secure their overdrafts by depositing collateral or by having some other large bank furnish a standing guarantee covering whatever overdrafts may occur. While the bank generally undertakes to carry overdrafts for those customers who enjoy this privilege, unless they exceed the maximum amount agreed upon, it reserves the right to call upon the correspondent to make good the overdraft at any time.

In connection with a reimbursement account the foreign correspondent makes arrangements to overdraw its account, but it provides the New York bank with some means of reimbursement for the amount overdrawn. Usually the foreign correspondent arranges for the American bank to reimburse itself by drawing a draft upon another bank. The bank discounts this draft with its foreign discount department and uses the proceeds to restore the overdrawn account. Another

method of reimbursement is for the American bank to discount, in accordance with standing instructions, certain unmatured bills which it is holding in portfolio for the foreign bank. Some foreign customers who desire to maintain a balance of a certain minimum size make use of this same arrangement for having their accounts restored when they fall below the stipulated amount.

### Special Instructions

In addition to watching for overdrafts, there is the important duty of caring for other standing and special instructions given by depositors. Many customers request the bank to notify them by cable or by letter when overdrafts occur. Others request that cable messages showing the size of their balances be sent them at stated intervals. Some banks have instructions to the effect that whenever their balances exceed a certain amount the excess is to be remitted to them or to some other correspondent. Instructions of this sort are noted opposite the account in the ledger and also in the card file to make sure they receive the proper attention. Matters requiring attention because of these instructions are, of course, referred to the proper officer for action.

### Statements of Account

The statement of the foreign account (Form 87) is similar to that of the domestic. While the statement is in the process of preparation it serves the important function of giving information for answering inquiries and acknowledging advices received from abroad. In this same connection outgoing advices of debit and credit which the bank according to the custom of international banking sends to its correspondents when it debits or credits their accounts, are inspected by the statement clerks before they are mailed. As an additional safeguard against charging an account more than once for



IN ACCOUNT WITH THE NATIONAL CITY BANK OF NEW YORK E & O E.											
BANK OF NEW YORK New York, N.Y.		BRANCHED AT Antwerp, Belgium.		V		VALUE	DEBIT	CREDIT	BALANCE	INTEREST NUMBERS DATE MONTH YEAR	
MAY 25									179,579.30	1	1796
26				10	Mar.			25,000.00		"16"	4000
				24				10,000.00		"2"	200
				25			12,000.00			"1"	"120
				26				576.00			
				26				10,724.98			
				26			24,376.90				
				26			5,000.00				
				26			11,170.00				
				26			5,257.70				
				26			5,854.00				
				26			29,075.62				
									139,146.03	1	1391

Notes:

- \* Interest allowed the Foreign Bank on the funds which were not received until the date of entry Interest is allowed from the Value Date until the date of entry to the account.
- \*\* Interest to be deducted by the Bank for the Transfer of March 25th Value Date which was not entered against the account until March 26.

IMPORTANT			
PLEASE FILL OUT THE ATTACHED BLANK AND RETURN TO THE AUDITOR IN THE ENCLOSED ENVELOPE			

the same item, all duplicate drafts are examined by the accounts current clerks before they are approved for payment.

A difference in the procedure in international banking and in domestic banking is to be noted in the disposition made of the drafts and other paid vouchers. It will be recalled that in the domestic work the paid checks and other instruments are returned to the customer along with the periodical statement of account. On the other hand, except in the case of a few banks which have filed specific requests for such service, the paid drafts are not returned to foreign correspondents. These paid drafts are filed by the paying bank and they are useful material for proving that payment has been made when duplicates or other copies are presented and for obtaining copies of indorsement for identification of holders who have no means of identification other than the fact that they have cashed a foreign draft at the bank at some time in the past.

### Interest on Accounts

Interest on deposits is quite generally allowed in foreign banking and the rates are by custom slightly better than in the domestic field. The work of computing and accounting for interest is done by the statement clerks and the interest clerks. In arriving at the amount of interest to be allowed on an account the Staffel system is used. This system is briefly as follows. Interest numbers are obtained by multiplying the balance of the account by the number of days it remains unchanged. At the end of the interest period these interest numbers are added, multiplied by the rate of interest allowed on the given account, and this product divided by 360. The quotient is the credit interest of the given account. If the account has been overdrawn during any portion of the interest period, by custom prevailing in international banking the bank is permitted to charge interest on the amount of

overdraft at a higher rate. The difference between the debit interest calculation on the overdrafts and the credit interest calculated on credit balances gives the net interest. Interest clerks attached to the department check the calculations of the accounts current clerks and report the amount of expense incurred on account of interest to the voucher register. In the voucher register the amount is charged to the Interest Paid account and the various ledgers are credited.

### Indirect Drawings

In the discussion of foreign drafts it has been said that the New York bank occasionally draws drafts upon foreign banks with which it has no direct connections. Likewise foreign banks which are not customers of the American bank sometimes draw drafts upon it. When a foreign bank draws a draft in this way it sends the usual advice. In the advice the drawer bank instructs the drawee as to the method which the latter shall use in order to reimburse itself for this outlay.

Reimbursement for indirect drawings is generally to be made by having the drawee bank charge the account of some bank which is a correspondent of both itself and the drawer, although it is occasionally made by having the drawee bank draw a draft in its own favor upon some bank designated by the drawer. In case an indirect drawing is to be charged to the account of some one of the bank's foreign correspondents, that correspondent sends an advice authorizing the charge to be made. The drawee bank honors the drawing only after it has received this advice. If a reimbursement draft is drawn, it is made large enough to include the face of the drawing and interest for the time required for collection. Then it is discounted with the foreign discount department and the proceeds are used for the purpose of meeting the foreign bank's draft.

### Clean Credits

Clean credits not having a definite stated face value are handled by the bookkeepers. Under a clean credit of this sort a correspondent advises the New York bank that the beneficiary will draw approximately a certain amount and requests the latter bank to honor such drafts and reimburse itself in an approved way, usually by charging the advising bank's account.

When a clean credit is opened by a foreign correspondent a record of the credit is made in the clean credits ledger. To each credit there is assigned a serial number under which it is recorded in the ledger. The entry contains the name of the beneficiary of the credit, by whom issued, credit number of the issuing bank, the expiration date of the credit, if any, the method to be employed by the bank in reimbursing itself, the approximate amount of the credit, and the method of opening it—whether by letter or by cable.

As drafts are drawn on the bank by the beneficiary and paid the bank reimburses itself according to instructions—almost invariably by charging the account of the bank opening the credit. As the drafts are paid the amounts of payment are entered in the ledger. When the maximum amount to be drawn has been reached or the time limit has expired, the credit is ruled off and closed.

### Foreign Drafts Drawn upon Domestic Correspondents

To assist its foreign correspondents in meeting the demands which their customers make upon them for drafts drawn upon any cities in the United States, Canada, the Hawaiian Islands, Cuba, etc., in which the foreign banks do not have correspondents, the New York bank makes arrangements for these banks to draw upon its own correspondents in these cities. To each foreign bank enjoying this privilege the American bank sends a list of the correspondents upon which the foreign institution

may draw When it draws a draft in this manner the foreign drawer bank advises the New York bank of its action, giving full particulars in the advice, and asks the latter to honor the draft and reimburse itself for its outlay by any method which it desires The drawee correspondent usually reimburses itself by sending the paid draft to the New York bank for credit or by drawing a draft upon the latter The profit to the New York bank is interest upon the face of the draft from the time that the advice is charged to the account of the foreign bank until reimbursement is made to the drawee bank

In addition to the accounts of foreign depositors, a large number of miscellaneous accounts are kept by the foreign bookkeepers (1) general accounts, and (2) accounts which help to make up the control accounts for the foreign ledgers

### General Accounts

In anticipation of what is to be said in the following chapter, it may be stated at this point that each account of the bank other than those of customers, that is, each general account, is kept in a descriptive ledger. Some of these descriptive ledgers are kept by the general bookkeepers, while others are kept by the customers' bookkeepers In these descriptive ledgers detailed entries of both debit and credit tickets are made In case the descriptive ledger containing a given account is kept in some department other than the general bookkeepers, the general bookkeepers department receives from the ticket journal department the tickets which are to be posted to the descriptive ledgers and it enters them in total to its control accounts, then they are passed to the department keeping the detail accounts

The general accounts kept by the foreign bookkeepers consist of the following Customers' Liability under Commercial Credits, Acceptances of this Bank, Advances to Customers, and Own Time Bills Payable Abroad

### Miscellaneous Accounts

Miscellaneous accounts kept by the foreign bookkeepers in much the same way as an account with a foreign bank or individual are such ones as: Prepaid Exchange, Brokerage (representing brokerage due to foreign exchange brokers), Unpaid Exchange, Foreign Collection account, Funds Segregated (representing funds set aside from customers' balances for the purpose of securing commercial credits opened for them), Funds Retained for Foreign Teller's Drafts, Sundries account (corresponding to the Cashier's account of the domestic division) Each of these accounts has been previously described and it is unnecessary to repeat the description at this point

### Official Records

In conjunction with the work of the foreign bookkeeper's department certain statistical records are prepared for the use of the officers of the foreign division Each day statements are made of the condition of the overdrafts and of the changes occurring in the larger balances These statements are forwarded to the daily meetings of the officers of the bank The officers of the various foreign districts also receive daily, weekly, and monthly statements of the overdraft balance of the accounts, total balances by foreign countries, number of accounts opened and closed during the period, and other important data relating to them.

## CHAPTER XXIII

### THE GENERAL ACCOUNTS

#### Nature and Purposes

Thus far the accounting for customers' balances and for the "due from" foreign accounts has been described. These balances, of course, correspond to the accounts payable and the accounts receivable of the ordinary business concern. The aggregate balances of these accounts constitute only a small part of the balance sheet of the bank. There yet remain to be considered the so-called general accounts. These include the resources and liabilities other than balances due from and due to customers, the profit and loss or nominal accounts, and the capital accounts of the bank.

Keeping the general accounts of the bank includes.

1. Accounting for the expense of the bank
2. Posting to the descriptive and subsidiary ledgers.
3. Keeping the general ledger
4. Preparing a daily statement of condition
5. Drawing up profit and loss statements and closing the ledger
6. Preparing reports and statistics for the clearing house, the Comptroller of the Currency, and the officers of the bank

#### Expenses

Original entry material for the general ledger yet to be considered consists of the expense records. The expenses of the bank are kept on an accrual basis. Under this system the total expenses for the year are estimated and distributed over

the year's operations by equal monthly instalments regardless of the amount actually paid for each month

The expenditures of a bank are of three classes

- 1 Interest paid
- 2 Taxes
- 3 General expenses

#### 1. Interest Paid

*On Deposit Balances* The method of accruing interest paid on depositors' accounts has already been described in connection with the work of the interest department and the foreign bookkeepers. By way of summary it should be said that the total interest accrued on depositors' balances is charged to the Interest Paid account and credited to Reserve for Interest. The Interest Paid account, which enters the profit and loss statement of the bank, thus consists of the figure actually accrued rather than that actually paid. Interest payments are charged to the Reserve for Interest account the balance of which is a liability showing interest accrued but unpaid.

*On Borrowed Money and Bonds.* The other item of interest is interest paid on borrowed money and on borrowed bonds. Money may be borrowed at the federal reserve bank on a rediscount basis or on a loan basis. On the loan basis the bank borrows on its note secured by collateral. The interest paid on such a note is charged directly to the "Interest Paid on Borrowed Money" account. On rediscounts the bank pays the discount in advance to the federal reserve bank, just as do borrowers to the domestic discount department of the bank itself. The amounts so paid are charged to the "Prepaid Expense—Discount on Borrowed Money" account. At the close of the month the amount accrued, in other words the amount actually earned by the federal reserve bank on this bank's rediscounts, is transferred from the Prepaid Expense Discount on Borrowed Money account to the Interest Paid



on Borrowed Money account This is a subsidiary account which is closed into the general Interest Paid account The Interest Paid account thus contains a record of interest actually accrued, while the Prepaid Expense—Discount on Borrowed Money account when adjusted at the end of the month is an asset account which shows interest prepaid for future use of borrowed money. Similarly, interest accrued on borrowed bonds during the month is charged to Interest Paid and credited to Reserve for Interest

### 2 Taxes

The bank is concerned with four classes of taxes

- 1 The tax on income
- 2 The state tax on capital stock
- 3 The federal tax on circulation
- 4 The city tax on real estate

*Income Tax* The national income tax, the excess profits tax, and corporation tax which a bank must pay vary with the frequent changes made in these laws The bank can generally determine one year in advance what its rate of taxation will be Knowing the profits and other factors upon which these taxes are based, the amount of tax to be paid can be arrived at fairly definitely

*State Tax on Capital Stock.* Under the laws of the United States,<sup>1</sup> the states in which a national bank is located are permitted to tax the shares of stock of that bank as personal property of the owners The system used in New York State may be described as follows Each bank is required to report annually to the assessors of the local tax district the names of the stockholders, their addresses, and the number of shares of stock owned by each, the capital, surplus, undivided profits, and other data These local assessors make the assessment

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<sup>1</sup> Section 5219, United States Revised Statutes

to the owners in the tax district where the bank is located regardless of their residence. The method of arriving at the value of the share is prescribed by law, the sum of the capital, surplus, and undivided profits is divided by the number of shares. The law also prescribes the rate of tax at 1 per cent of this assessed value and it requires the bank to act as agent of the state in the collection of the tax, paying the tax out of its profits and having a lien upon the shares of stock or other property of the stockholder in its hands.

*Federal Tax* By federal law each national bank is required to pay semiannually  $\frac{1}{4}$  of 1 per cent on the average amount of circulation it has outstanding secured by United States 2 per cent bonds, and  $\frac{1}{2}$  of 1 per cent on the average circulation secured by other United States bonds. The tax applies only to those notes strictly outstanding in circulation. It is payable in the months of January and July. Ten days after the first days of these months each bank is required to make a return under oath of its president or cashier to the Treasurer of the United States of the average amount of its notes in circulation for the 6 months preceding the first day of January or July.

*City Tax* The above-cited federal statute also permits the state, county, and municipality wherein a national bank is located to tax the real property of the national bank to the same extent, according to its value, as other real property is taxed. In New York State the bank's real property is subject to local taxation and no deduction is allowed from the value of the shares of stock on account of these taxes on real estate. The 1 per cent tax on shares of stock is so far below the general property tax rate that this double taxation is deemed to work no great injustice. This tax is payable semiannually.

The total taxes which it is estimated that the bank must pay for the year are divided into twelve equal parts. Each month one of these parts is charged to the Taxes Paid account.

and credited to Reserve for Taxes account. The balance of the Taxes Paid account enters the monthly profit and loss account of the bank, thereby charging Accrued Taxes for the month against current earnings. The tax payments are charged to Reserve for Taxes account. At any time the balance of this account is a liability representing taxes accrued but not due nor paid.

### 3. General Expenses

The general expenses of the bank are of two classes: salaries, and other expenses. Salaries are paid promptly and in full, of course, during the current month, hence there is no accrual to be cared for. Other expenses are estimated on a budget basis. Knowing the cost of operating an activity of the bank during past years and the plans for expanding or contracting that activity for the current year, it is comparatively easy to set up a budget figure covering the expenses of that activity for the coming year. For every activity the cost of which is classed as a general expense item, a budget figure is set up. The total yearly budget arrived at in this way is divided into equal monthly parts. Each month the figure obtained in this way is added to the salaries paid and the total charged to General Expenses Paid and credited to Accrued Expense account. The General Expenses Paid account is closed into Profit and Loss, just as are the Interest Paid and the Taxes Paid accounts, thereby charging expenses accrued during the current month against current earnings. As general expense bills are actually paid they are charged to the Accrued Expense account, the balance of which represents expenses accrued but unpaid.

### Voucher System for Handling Expenses

In handling expense payments the bank uses the voucher system, the use of which may be illustrated by tracing the

progress of an order for the purchase of supplies through the system

*Supplies* An order for supplies commonly has its origin in a requisition which is approved by the proper department head and division head and by the comptroller of the bank. This requisition passes to the purchasing department where it serves as an authorization to purchase the supplies enumerated. This department draws up its purchase order in triplicate, the original is sent to the merchant from whom the goods are to be bought, the duplicate together with the requisition is forwarded to the bookkeepers in charge of the expense accounts, who file these memoranda alphabetically by name of the merchant, and the triplicate is sent to the receiving-room so that incoming deliveries may be checked against the order. When the bill for the goods arrives its accuracy is verified by means of the copy of the corresponding purchase order and entered on a serially numbered voucher card.

On the card is entered the date of the transaction and the journal entry arising from it. This journal entry consists of a debit to one of the expense accounts of the bank (General Expenses Paid, Building and Equipment, Prepaid Expense, Customers' Expense Fund, or Branches) and a credit to Accrued Expense. The various memoranda supporting the transaction are clamped securely to the voucher card and the whole transaction is presented to the comptroller of the bank for approval. After the transaction has been approved the voucher card serves as the basis for an entry to the voucher register, then the card together with supporting documents is filed away as a permanent record of the transaction.

If the bill is due a voucher check is drawn in payment. This check is of the usual type, containing space for a list of the items to which the payment applies, i. e., it is a sort of combined statement and check. Should the order be a very extensive one a separate memorandum of the items paid

is attached to the check. The check and the whole transaction are thereupon presented to an officer who reviews the transaction and signs the check, the auditors next ascertain that all is in order and payment is mailed to the creditor. When indorsed by him and returned to the bank the voucher check constitutes a receipt for the amount paid. Checks drawn in payment of these bills are charged to the Accrued Expense account and credited to the Cashier's Check account.

In the case of merchants from whom the bank makes frequent purchases the bills are generally paid by a single check on the first and fifteenth of each month. The bills received from a particular creditor are listed and the charges distributed upon a single voucher card and they are all passed upon by the comptroller at one time. Those bills which carry a cash discount are filed in a tickler as of the last day on which the discount may be taken advantage of, and on that day they are paid in the usual manner.

*Pay-Roll, etc.* Other expenses are handled in a way similar to supplies. The pay-roll, for example, is handled as follows: The paymaster presents a requisition to the bookkeepers showing the distribution of the salaries by departments, the bookkeepers copy this classification of the pay-roll upon the usual voucher card, have the transaction approved by the organization department, and write a check for the total. This check is then given to the petty cashier who obtains currency with it from the paying teller and makes up the pay envelopes of the employees. Upon receiving his pay envelope each employee signs a receipt which is filed as evidence that payment has been made.

Expenses such as fees for credit information service, insurance, clearing house membership, etc., which have to be paid in advance, are charged to the Prepaid Expense account at the time of payment. Each of these items is divided into equal parts according to the number of months over which

the payment extends and posted in a special tickler expense ledger. At the end of each month the amounts used up are transferred from Prepaid Expense to General Expenses Paid by means of voucher entries.

### **Voucher Register**

Each voucher is recorded in the voucher register (Form 88) which serves as a journal from which the entries are posted to the general books. In this book is recorded the voucher number, the date, to whom issued, and the journal entry covering the transactions. This entry consists of a credit to Accrued Expense for the total amount of the voucher and debits to the proper divisions of the expense accounts as shown upon the voucher card. In addition to expense payments certain journal entries are passed through the voucher register. These are for the purpose of recording adjustments, closing entries, and certain confidential entries originating with the administration of the bank. At the end of the day a proof (Form 89) is taken from the voucher register and forwarded to the general bookkeepers for posting to the control accounts of the general ledger.

### **Expense Ledgers**

In addition to the paid voucher files, descriptive ledgers, as illustrated in Form 90, are kept for the various expense accounts. These are separate ledgers for general expense, prepaid expense, and branches.

The general expense item is divided into three classes: general, domestic, and foreign. In so far as is practicable, each of these is subdivided so that expense figures to show the cost of operating each department in the bank are obtained. In order that each item of expense may be readily referred to on the records each subdivision has a distinctive number. Thus the account Depreciation on Building is indicated by

THE NATIONAL CITY												
VOUCHER REGISTER AND												
DATE	VOUCHER NUMBER	EXPLANATION	CREDIT				DEBIT				BALANCE	
			ACCOUNT	AMOUNT	DEBIT	CREDIT	ACCOUNT	AMOUNT	DEBIT	CREDIT		
1916	1	Wm. H. H. Co.										
1916	2	Wm. H. H. Co.										
1916	3	Wm. H. H. Co.										
1916	4	Wm. H. H. Co.										
1916	5	Wm. H. H. Co.										
1916	6	Wm. H. H. Co.										
1916	7	Wm. H. H. Co.										
1916	8	Wm. H. H. Co.										
1916	9	Wm. H. H. Co.										
1916	10	Wm. H. H. Co.										
1916	11	Wm. H. H. Co.										
1916	12	Wm. H. H. Co.										
1916	13	Wm. H. H. Co.										
1916	14	Wm. H. H. Co.										
1916	15	Wm. H. H. Co.										
1916	16	Wm. H. H. Co.										
1916	17	Wm. H. H. Co.										
1916	18	Wm. H. H. Co.										
1916	19	Wm. H. H. Co.										
1916	20	Wm. H. H. Co.										
1916	21	Wm. H. H. Co.										
1916	22	Wm. H. H. Co.										
1916	23	Wm. H. H. Co.										
1916	24	Wm. H. H. Co.										
1916	25	Wm. H. H. Co.										
1916	26	Wm. H. H. Co.										
1916	27	Wm. H. H. Co.										
1916	28	Wm. H. H. Co.										
1916	29	Wm. H. H. Co.										
1916	30	Wm. H. H. Co.										
1916	31	Wm. H. H. Co.										
1916	32	Wm. H. H. Co.										
1916	33	Wm. H. H. Co.										
1916	34	Wm. H. H. Co.										
1916	35	Wm. H. H. Co.										
1916	36	Wm. H. H. Co.										
1916	37	Wm. H. H. Co.										
1916	38	Wm. H. H. Co.										
1916	39	Wm. H. H. Co.										
1916	40	Wm. H. H. Co.										
1916	41	Wm. H. H. Co.										
1916	42	Wm. H. H. Co.										
1916	43	Wm. H. H. Co.										
1916	44	Wm. H. H. Co.										
1916	45	Wm. H. H. Co.										
1916	46	Wm. H. H. Co.										
1916	47	Wm. H. H. Co.										
1916	48	Wm. H. H. Co.										
1916	49	Wm. H. H. Co.										
1916	50	Wm. H. H. Co.										
1916	51	Wm. H. H. Co.										
1916	52	Wm. H. H. Co.										
1916	53	Wm. H. H. Co.										
1916	54	Wm. H. H. Co.										
1916	55	Wm. H. H. Co.										
1916	56	Wm. H. H. Co.										
1916	57	Wm. H. H. Co.										
1916	58	Wm. H. H. Co.										
1916	59	Wm. H. H. Co.										
1916	60	Wm. H. H. Co.										
1916	61	Wm. H. H. Co.										
1916	62	Wm. H. H. Co.										
1916	63	Wm. H. H. Co.										
1916	64	Wm. H. H. Co.										
1916	65	Wm. H. H. Co.										
1916	66	Wm. H. H. Co.										
1916	67	Wm. H. H. Co.										
1916	68	Wm. H. H. Co.										
1916	69	Wm. H. H. Co.										
1916	70	Wm. H. H. Co.										
1916	71	Wm. H. H. Co.										
1916	72	Wm. H. H. Co.										
1916	73	Wm. H. H. Co.										
1916	74	Wm. H. H. Co.										
1916	75	Wm. H. H. Co.										
1916	76	Wm. H. H. Co.										
1916	77	Wm. H. H. Co.										
1916	78	Wm. H. H. Co.										
1916	79	Wm. H. H. Co.										
1916	80	Wm. H. H. Co.										
1916	81	Wm. H. H. Co.										
1916	82	Wm. H. H. Co.										
1916	83	Wm. H. H. Co.										
1916	84	Wm. H. H. Co.										
1916	85	Wm. H. H. Co.										
1916	86	Wm. H. H. Co.										
1916	87	Wm. H. H. Co.										
1916	88	Wm. H. H. Co.										
1916	89	Wm. H. H. Co.										
1916	90	Wm. H. H. Co.										
1916	91	Wm. H. H. Co.										
1916	92	Wm. H. H. Co.										
1916	93	Wm. H. H. Co.										
1916	94	Wm. H. H. Co.										
1916	95	Wm. H. H. Co.										
1916	96	Wm. H. H. Co.										
1916	97	Wm. H. H. Co.										
1916	98	Wm. H. H. Co.										
1916	99	Wm. H. H. Co.										
1916	100	Wm. H. H. Co.										

Form 88 (a) Voucher Register (left half). (Size 17 x 18½)





PROOF		
MADE BY <i>Wm H. Edwards</i> CHECKED BY <i>G. O. Evans</i>		
DATE <i>April 16 1927</i>		
VOUCHER DEPARTMENT		
DEBIT	ACCOUNTS	CREDIT
	SALES RECEIVABLE - DEPOSIT	910
	TREASURY	860.58
	RECEIVABLES	95.25
7.50	TOTAL	1,865.83
660.00	SALES DEPOSIT - DEBIT	2,500.00
1,481.79	RECEIVABLES	7.00
	SALES DEPOSIT - DEBIT	
	RECEIVABLES	
	SALES DEPOSIT - DEBIT	
	RECEIVABLES	
1,121.79	TOTAL	2,507.00
1,588.79	RECEIVABLES	1,481.72
150.62	SALES DEPOSIT - DEBIT	2.50
24.99	RECEIVABLES	
1,588.79	SALES DEPOSIT - DEBIT	
189.12	RECEIVABLES	1,987.95
1,777.91	TOTAL	3,975.91
1,488.12	RECEIVABLES	7,581.79
1,987.15	SALES DEPOSIT - DEBIT	
	RECEIVABLES	
	SALES DEPOSIT - DEBIT	
	RECEIVABLES	
	SALES DEPOSIT - DEBIT	
	RECEIVABLES	
1,777.15	TOTAL	7,581.79
199.60	RECEIVABLES	171.29
185.58	SALES DEPOSIT - DEBIT	
	RECEIVABLES	
	SALES DEPOSIT - DEBIT	
	RECEIVABLES	
	SALES DEPOSIT - DEBIT	
	RECEIVABLES	
305.18	TOTAL	2,152.28
1,481.79	RECEIVABLES	925.18
1,481.79	SALES DEPOSIT - DEBIT	
	RECEIVABLES	
	SALES DEPOSIT - DEBIT	
	RECEIVABLES	
	SALES DEPOSIT - DEBIT	
	RECEIVABLES	
1,481.79	TOTAL	925.18
1,481.79	RECEIVABLES	860.58
1,481.79	SALES DEPOSIT - DEBIT	860.58
1,481.79	TOTAL	1,721.16
245.65	RECEIVABLES	509.00
	SALES DEPOSIT - DEBIT	
	RECEIVABLES	
	SALES DEPOSIT - DEBIT	
	RECEIVABLES	
	SALES DEPOSIT - DEBIT	
	RECEIVABLES	
245.65	TOTAL	509.00
1,481.79	RECEIVABLES	1,481.79
1,481.79	SALES DEPOSIT - DEBIT	1,481.79
1,481.79	TOTAL	2,963.58

Form 89 Accounting Department's Proof (Size 11 x 16½)



the number G 93, the letter G representing that the account belongs in the general classification, the figure 9 showing that the expense applies to the building, and the figure 3, the subclass depreciation. Some expenses, such as stationery and supplies, are kept in one account, but supplementary records showing the distribution by department are maintained. Once a month postings are made to these ledgers from recapitulation sheets which are built up from the voucher register entries.

### Subsidiary Ledgers

In the accounting system of a bank, as in any other large business concern, details of the various accounts are far too voluminous to be kept in the general ledger the function of which is to show all the accounts making up the bank's financial position. Details of each account are kept rather in descriptive ledgers. The accounts of the general ledger are control accounts each of which is supported by one or more descriptive ledger accounts. Some of the descriptive ledgers are kept by the general bookkeepers of the bank, others are kept by the foreign bookkeepers, as has already been indicated, and still others by the operating departments, according to convenience.<sup>2</sup>

<sup>2</sup> The accounts kept in the descriptive ledgers of the general bookkeeper's department consist of the following

Advanced to Customers on	Travelers' Letters of Credit
" " "	" Export Bills
" " "	" Foreign Shipments
" " "	" Domestic Shipments
" " "	" Arrival Drafts
Bills Discounted—Foreign	
Suspense	
Accounts Receivable	
Prepaid Expense	
Interest Earned But Not Collected	
Lawful Reserve with Federal Reserve Bank	
Foreign Currency (classified by kinds)	
Coupons	
Customers' Liability Acceptances of National City Bank under Commercial Credits—Domestic	
Customers' Liability Acceptances of National City Bank under Commercial Credits—Foreign	
Undivided Profits	
Interest	
Discount	
Exchange	
Commission	



to accounts kept in detail by the general bookkeepers, however, are retained, posted, and sent to the record files. To enter such tickets separately would be a task of some magnitude. For this reason tickets for certain of the accounts are posted to the descriptive ledgers by batch totals and the adding machine lists showing the tickets in each batch are labeled and posted in a supplementary book for ready reference. Tickets for other accounts, such as the Cashier account, the Lawful Reserve with the Federal Reserve Bank of New York account, etc., however, are entered in a descriptive ledger in detail; that is, the number, the amount, and any remarks which will be of service in identifying the transaction are recorded for each ticket.

### **Cashier's Check Account**

Among the descriptive ledger accounts of the general bookkeeping department the Cashier's Check account is kept in a distinctive way. Credits to this account are posted to the general bookkeepers descriptive ledger by means of credit tickets coming from the departments issuing checks, while debits are posted from the proof of the check desk department. Further details of the account are kept by means of carbon copies of the checks themselves. These duplicates are received by the general bookkeepers from the operating departments at the time the checks are issued, they are proved against the corresponding credit tickets and filed numerically according to the department of issue. When the checks are paid by the bank they come to the general bookkeepers by way of the check desk. In the general bookkeeping department these original copies are proved against the check desk charge made to the Cashier's Check account, then the corresponding duplicates are withdrawn from the outstanding file and filed in a paid file. By this system details of the balance of the Cashier's Check account, which represents checks outstanding,

are portrayed by the carbon copies of the checks themselves.

### **Federal Reserve Bank Collection Account**

Another descriptive ledger account which is kept in a distinctive way is the Federal Reserve Bank Collection account. This account represents cash items which have been sent to the federal reserve bank for collection but which have not yet matured into reserve. It will be recalled that under the regulations of the federal reserve banks items sent to them for collection are classified on the basis of time required for collection into those of immediate availability and those which will become available after 1, 2, 4, and 8 days, respectively. Sendings which are immediately available are, of course, charged by the sending bank to its Lawful Reserve account and they do not enter this collection account. Other sendings, however, are debited to the Federal Reserve Bank Collection account temporarily and at maturity they are transferred from this account to the Lawful Reserve account.

The Federal Reserve Collection account is kept in a specially ruled ledger in which the vertical columns show the items maturing on each day of the month and the horizontal lines show the entries classified by day's availability—1, 2, 4, and 8 days, respectively. The original postings are made from the reports prepared by the transit department. The arrangement of the ledger is such that it serves as a tickler showing the amounts which become available for reserve each day. Transfer of the proper amount from this account to the Lawful Reserve account is made by means of tickets prepared by the general bookkeepers.

The method of using this account may be illustrated by an example. Suppose the account was opened on April 15 and the sendings of the transit department between April 15 and April 24 were as follows.

## SENDINGS

Date	1 day items	2 day items	4 day items	8 day items
April 15	\$2,500,000	\$2,000,000	\$1,750,000	\$500,000
16	3,000,000	2,500,000	1,650,000	200,000
17	2,750,000	4,000,000	1,900,000	300,000
18	3,500,000	3,250,000	2,000,000	450,000
19	3,000,000	3,000,000	800,000	375,000
20	4,000,000	2,950,000	900,000	600,000
21	3,750,000	3,300,000	750,000	500,000
22	3,250,000	3,450,000	850,000	480,000
23	4,000,000	2,750,000	900,000	510,000
24	3,500,000	3,250,000	950,000	505,000

The corresponding entries in the Collection account would be as follows (the date on which cash entry was made is indicated by the figures in parenthesis)

	April 16	April 17	April 18	April 19	April 20
8	.	.	.	.. .. (15)	.. .. (16)
4	..	.. .. (15)	(16)	\$1,750,000 (17)	\$1,650,000 (18)
2	(15)	\$2,000,000 (16)	\$2,500,000 (17)	4,000,000 (18)	3,250,000 (19)
1	\$2,500,000	3,000,000	2,750,000	3,500,000	3,000,000
Transfer Total	<u>\$2,500,000</u>	<u>\$5,000,000</u>	<u>\$5,250,000</u>	<u>\$9,250,000</u>	<u>\$7,900,000</u>
	April 21	April 22	April 23	April 24	April 25
8	.	.	(15) \$ 500,000	(16) \$ 200,000	(17) \$ 300,000
	(17)	(18)	(19)	(20)	(21)
4	\$1,900,000 (19)	\$2,000,000 (20)	800,000 (21)	900,000 (22)	750,000 (23)
2	3,000,000 (20)	2,950,000 (21)	3,300,000 (22)	3,450,000 (23)	2,750,000 (24)
1	4,000,000	3,750,000	3,250,000	4,000,000	3,500,000
Transfer Total	<u>\$8,900,000</u>	<u>\$8,700,000</u>	<u>\$7,850,000</u>	<u>\$8,550,000</u>	<u>\$7,300,000</u>

At the end of each of the days indicated at the head of the columns, tickets would be drawn debiting Lawful Reserve with the Federal Reserve Bank and crediting Federal Reserve Bank Collection account for the total amount of the column. For convenience one section of the account is kept in this way

for the items sent to the Federal Reserve Bank of New York and another section for the direct sendings, that is, those items sent direct to out-of-town federal reserve banks and branches for credit to the sending bank's account with the New York Federal Reserve Bank

### **Subsidiary General Ledger**

The customers ledgers have the same relation to the general ledger as do the descriptive ledgers, that is, they contain the details of accounts which appear in the general ledger in the form of control accounts. The general ledger accounts which control these ledgers are the Due to Domestic Banks and Bankers, Due to Foreign Banks and Bankers, Individual Deposits—Domestic, and Individual Deposits—Foreign. This ledger is of the Boston type. These accounts are built up by means of recapitulation sheets to be presently described. These four accounts, however, do not show details sufficient to check the accuracy of the depositors ledgers. To accomplish this purpose a subsidiary general ledger containing an account for each depositors ledger is used. This ledger is of the Boston type. Postings are made to it from the reports or proofs of the ticket journal department, the check desk department, and the operating departments of the bank.

The credits made to the accounts of the subsidiary general ledger are as follows: (1) total deposits as reported on the proofs of the receiving, the mail, and foreign tellers; (2) proceeds of collections as reported by the note teller and the city collection department, and (3) proceeds of loans and discounts as reported by the loan and the discount departments. The debits arise in the following manner: (1) items charged to the accounts of collecting banks as reported by the transit department, (2) checks and other items charged to customers' accounts according to the check desk proof, and (3) checks certified according to the proof of the certification department.



In addition to these debits and credits there is the proof of the ticket journal department which includes all the debits and credits to customers' accounts made by means of double tickets. Each day each ledger bookkeeper of the domestic and the foreign bookkeeping department reports to the general bookkeeper the total balance of his ledger which must agree with the control figures of the subsidiary general ledger.

### The General Ledger

The general ledger of the bank contains controls over all the accounts of the institution. In this book all the accounts of the bank are drawn together for the first time. It is, so to speak, the apex of the accounting system. This fact may be clearly shown by examining the structure of a single account in the general ledger, e.g., the account "Due to National Banks." The entries to this account on the general ledger for a given day consist of a single debit, a single credit entry, and a balance without description of any kind. Figures contained in this balance represent the aggregate of nine control accounts in the subsidiary general ledger. These control accounts represent nine ledgers kept in the domestic bookkeeping department, and these nine ledgers contain some fifteen hundred active accounts with correspondents. Other accounts in the general ledger are similar in structure to the Due to National Banks, some control as many as one thousand accounts, others only one.

The general ledger is of the Boston type. One volume is kept for resources, another for liabilities. The material from which postings are made to the general ledger is of two kinds: that which concerns the customers' accounts, and that which applies to the other or general accounts. The entry material for the customers' accounts consists entirely of the departmental proofs, or reports of debits and credits sent to the bookkeepers, which have been mentioned in connection

with the operating departments of the bank<sup>3</sup> each of which shows the total charge and the total credit sent by the particular department to each customers ledger with which that department has had relations during the day. After the figures of these proofs have been posted to the control accounts in the subsidiary general ledger, they are assembled upon a recapitulation sheet. Upon these sheets the figures are grouped under headings appearing in the general ledger, Individual Deposits—Domestic, National Bank Deposits, State Bank Deposits, Trust Company and Savings Bank Deposits, Foreign Bank Deposits, Individual Deposits—Foreign, Time Deposits—Foreign, Due to Branches, Due from Branches, Due from Banks—Foreign, Due from Banks—Domestic, Time Deposits—Domestic. Posting to the general ledger, so far as customers' accounts are concerned, consists in transcribing the totals shown on these recapitulation sheets to the corresponding accounts in the general ledger.

The entry material for the general accounts consists of departmental proofs and recapitulation sheets made up from the debit and credit tickets which come direct to the general bookkeepers for entry.

As a general rule departmental proofs do not contain material for the general ledger. The proofs of most of the departments consist of two parts—one a detailed report of debits and credits sent to the depositors ledgers, the other a record of debits and credits to cash and cash items. The reports of debits and credits sent to the customers ledgers are posted through the recapitulation sheets just mentioned. So far as the entries to the cash account are concerned, it is the practice for all departments save the city collection department and the paying teller's department to complete the

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<sup>3</sup> Receiving teller, mail tellers, city collection department, note teller, transit department, foreign tellers, loan department, discount department, certification department, ticket journal, coupon collection department, check desk, and accounting department.

day's work without any cash or cash items on hand. Under such a system the paying teller's proof shows the changes in the cash account of the bank and the items for the clearing house at the next day's session, and the proof of the city collection department shows other cash items in the process of collection, or the hold-overs. The debits and credits to Cash shown on the paying teller's proof are posted to the Cash account in the general ledger, the clearing house figure on this proof to the items for the Clearing House account, while the hold-overs shown on the proof of the city collection department are posted to the Country Checks and Cash Items account.

The proofs of the bond department, the loan department, the domestic discount department, and the accounting department, are exceptions to the general rule. These proofs contain records of all charges and credits to general accounts arising within these departments. Thus the proof of the domestic discount department contains entries to the following accounts: Bills Discounted—Domestic, Bills Purchased, Acceptances of the National City Bank—Foreign, Unearned Discount, Domestic Bills Rediscounted with Federal Reserve Bank, and many others. The figures pertaining to these general accounts are posted directly to the general ledger.

The recapitulation sheets for the tickets have already been described. The figures from these records are posted directly to the general ledger. The balances for the day are then extended and a trial balance taken.

### Daily Statement Book

The statement contained in the daily statement book of the bank consists of a trial balance taken from the general ledger. In addition to serving as a trial balance to show that the ledger is in balance, this statement is arranged to show the financial position of the bank for a given day and com-

parisons of these figures with those of preceding days. It must not, however, be confused with the financial statement of an ordinary business concern which consists of a balance sheet and a profit and loss statement. The daily statement of the bank is rather of the trial balance type—it contains the balances of all the accounts appearing in the general ledger with the exception of some of the less important ones which are grouped together for convenience. On one page of the statement book appear the ledger balances from the resources section of the general ledger; on the other side appear the balances from the liability section. The following is a list of the accounts arranged according to the classification in which they appear upon the daily statement of the bank.

### *Resources*

#### LOANS AND DISCOUNTS

Demand Loans

Demand Loans—Street

Demand Loans—Merchandise

Advances to Customers

Time Loans

Time Loans—Merchandise

Time Loans to Secure Bills Payable with Federal Reserve Bank

Bills Discounted—Domestic

Bills Discounted—Foreign

Bills Discounted to Secure U. S. Deposits

Acceptances of the National City Bank Discounted

Acceptances of the Other Banks Discounted

Suspense

Foreign Overdrafts

Total

#### SECURITIES

U. S. Bonds Deposited with Superintendent of Banks—State of New York

U. S. Bonds to Secure Trust Department Funds

U S Bonds to Secure Circulation  
 U S. Bonds to Secure U S Deposits  
 U S. Bonds to Secure War Savings Stamps and Thrift Stamps  
 U S Bonds to Secure State and Other Deposits  
 U S Bonds to Secure Bills Payable with Federal Reserve Bank  
 U S Bonds Loaned  
 U S Bonds on Hand  
 Other Bonds to Secure U. S Deposits  
 Other Bonds to Secure State and Other Deposits  
 Other Bonds Loaned  
 Other Bonds Sold with Agreement to Repurchase  
 Bonds to Secure Acceptance of Foreign Banks  
 Bonds Other than U. S Bonds to Secure Trust Department Funds  
 Bonds, Securities, etc  
 Federal Reserve Bank Stock (50 per cent paid)  
 Total

## OTHER RESOURCES

Banking House and Equipment  
 Accounts Receivable  
 Prepaid Expense  
 Interest Earned But Not Collected  
 5 per cent Fund Due from Treasurer of U S.  
 Country Checks and Cash Items  
 Cash in Bank  
 Lawful Reserve with Federal Reserve Bank  
 Due from Branches  
 Total  
  
 Due from Domestic Banks and Bankers  
 Due from Foreign Banks and Bankers  
 Due from Federal Reserve Bank—Collection Account  
 Exchanges for Clearing House  
 Checks on Other Banks in this City

## CUSTOMERS' LIABILITY—ACCEPTANCES OF

National City Bank under Commercial Credits  
 National City Bank to Create Dollar Exchange  
 Foreign Banks under Commercial Credits

TOTAL RESOURCES

*Liabilities*

## CAPITAL INVESTED

Capital Stock  
Surplus Fund  
Undivided Profits  
Surplus and Profits Net  
Total

## EARNINGS

Losses Recovered  
Interest  
Discount  
Exchange  
Commission  
Bond Profits  
Rent  
Difference and Fine Account  
Gross Earnings

## RESERVES

Reserved for Taxes  
Reserved for Interest  
Reserved for Depreciation—Building  
Total

## DEMAND DEPOSITS

U S Deposits  
Due to Domestic Banks and Bankers  
Due to Foreign Banks and Bankers  
Individual Deposits—Domestic  
Individual Deposits—Foreign  
Due to Branches  
Certified Checks  
Cashier's Checks  
Unpaid Dividends  
Cash Letters of Credit and Travelers' Checks  
Demand Certificates of Deposit  
Trust Department Funds—Individual  
Trust Department Funds—Corporate  
Total

## TIME DEPOSITS

Time Certificates of Deposit  
Other Time Deposits—Domestic  
Other Time Deposits—Foreign  
Total

## OTHER LIABILITIES

Discount Collected But Not Earned  
U S Bonds Borrowed  
Other Bonds Borrowed  
Bills Payable with Federal Reserve Bank  
Own Time Bills Payable Abroad  
Domestic Bills Rediscounted with Federal Reserve Bank  
Acceptances of other Banks Sold with Indorsement  
Foreign Bills Rediscounted Abroad  
Outstanding Circulation  
Accrued Expense  
Total

## ACCEPTANCES OF

National City Bank under Commercial Credits—Domestic  
National City Bank under Commercial Credits—Foreign  
National City Bank to Create Dollar Exchange  
Foreign Banks under Commercial Credits

## TOTAL LIABILITIES

For the information of the officers of the bank the following statistics are appended to the daily statement

## At the foot of the resources

Loans, Discounts, and Investments  
U S Deposits  
Gross Deposits  
Net Demand Deposits  
Time Deposits  
13 per cent of Net Demand Deposits  
3 per cent of Time Deposits  
Required Reserve  
Lawful Reserve with Federal Reserve Bank  
Excess Reserve  
Cash in Vault Available for Reserve

Cash in Vault for Reserve, per cent

Lawful Reserve with Federal Reserve Bank, per cent

At the foot of the liabilities

Country Deposits

New York City Trust and Savings Banks Deposits

Paper and Bonds Eligible for Rediscount and Hypothecation

Morning Clearings Debit

Morning Clearings Credit

### Computation of the Reserve Requirement

The bank is required at all times to maintain a reserve equal to at least 13 per cent of its demand deposits plus 3 per cent of its time deposits. To compute the demand deposits the gross deposits are first ascertained by adding together all deposit accounts, time deposits, government deposits, and overdrafts, and then making the following deductions: clearing house exchanges, checks on the other banks in this city, time deposits, government deposits, and due from domestic banks. Of this figure 13 per cent plus 3 per cent of the time deposits constitutes the bank's reserve requirement. By law this must consist of a deposit balance maintained with the federal reserve bank of the district. Should the bank permit its lawful reserve to fall below 13 per cent, it would be subject to a fine imposed by the Federal Reserve Board. Hence, should the indications from the clearing house point to a depletion of the bank's reserve, the tendency is forestalled by rediscounting at the federal reserve bank for relatively long-term needs (up to 90 days) or by borrowing at the same source on a short-term note secured by United States bond collateral for temporary needs.

The amount of reserve which the bank maintains to safeguard its deposits is closely watched by the officers of the bank. The record of the general bookkeeper's department, in addition to showing the actual Lawful Reserve account and the accretions which may be expected from maturing collec-



tions, indicate the decreases which will come from maturing bills payable at the federal reserve bank, changes which will result from the day's clearings, etc. From this data a monthly statement is submitted to the officers showing the amount and percentage of reserve each day as well as the monthly average

### **Profit and Loss Statements**

Each month statements showing the earnings, expenses, profits, and losses of the bank are prepared

The earnings and expenses of the bank have already been described in connection with the operating departments. Briefly, the earnings consist of discount earned on domestic and foreign discounts, interest earned on loans, bonds, foreign overdrafts, and on the foreign "due from banks," accounts, commissions of various kinds, exchange, and bond department "write-offs." The deductions from earnings consist of interest paid depositors and on rediscounts and loans at the federal reserve bank, and the various expenses of the bank.

The first step in computing the net profit of the bank is to arrive at the net earnings from operations. The term "net earnings from operations," as here used, denotes the difference between the ordinary earnings of the bank, i e., those from loaning money and performing such functions as opening commercial credits, acting as transfer agent, trading in foreign exchange, etc., less the ordinary expenses of the bank, such as interest payable, salaries, rent, etc. In the accounting system of the bank "net earnings from operations" has the same significance as similar terms used in the statements of other business concerns.

### **Monthly Interest Earnings Statement**

For convenience and for statistical purposes the earnings from domestic operations are shown separately from those coming from foreign operations. For the purpose of arriving

at the domestic earnings figure, a statement known as the monthly interest earnings statement is used. The principal earning of the bank is the interest which it receives from loaning its funds. Accordingly the first item of earnings shown on the statement is the net income from interest, or the net interest earnings figure. This is computed by deducting interest payable from interest receivable.

The interest receivable of the bank comes from three sources: discounts, loans, and securities. The method used in computing these earnings has been explained in the discussion of the work of the domestic discount, the loan, and the bond department. In the interest earnings statement simply the total monthly figure as shown on the records of these three departments is entered.

Interest payable represents that to be paid to depositors, to the federal reserve bank for funds loaned, and to owners of bonds who loan them to the bank. Methods of computing these have been described in the work of the interest department and in preceding paragraphs in this chapter. Interest paid depositors is classified for statistical purposes as domestic banks and individuals, domestic time deposits, certificates of deposit, United States government deposits, and trust deposits. The total interest paid depositors, plus interest on borrowed money, plus that paid on borrowed bonds, gives the total interest payable of the bank. The total interest receivable less the total interest payable gives the net interest earnings figure.

The second source of earnings to the bank from its domestic operations is its commissions. These are earned from the transfers and registrations of the transfer department, from the activities of the trust, the customers' securities, and the coupon paying department, from domestic commercial credits, etc. In addition to commissions the bank has a source of earnings in exchange, which represents the income from

making collections. Added to these two items of income is rent received for portions of the bank building occupied by outside concerns and income from sundry sources. The results obtained from computing commissions and exchange on an accrual basis would not justify the expense involved; hence they are kept on a cash basis, that is, only services actually paid for are taken into consideration.

The net interest earnings plus the total earnings from commissions, exchange, rent, and sundries shows the gross earnings from the ordinary operations of the domestic division of the bank. For statistical purposes this figure is compared with the total expenses of the bank. The excess is shown on the statement as excess interest earnings.

In addition to showing the excess interest earnings figure the monthly interest earnings statement is designed to show certain other important statistical data. On each item of interest receivable there is shown the average daily amount of funds invested in that particular type of investment, that is, the statement shows the average daily amounts of loans and discounts running and the average investment in stocks and bonds.

To arrive at these amounts, records are kept showing the amounts under discount, amounts running on loans, amounts invested in stocks and bonds, foreign overdrafts, due from foreign banks, and amounts running under foreign discount each day. At the end of the month simply an average of these amounts need be obtained. The average rate of earnings for each class during the month is also shown.

### **Interest Payable Section**

In the interest payable section average daily balances of the various classes of deposits for the month, as well as the average rates of interest paid thereon are shown. These balances are the interest balances already described in the work

of the interest department By virtue of the fact that the interest department's computations extend from the 25th of one month to the 25th of the next, while the statement covers a calendar month, the interest balances are corrected by deducting figures for the days of the preceding month which they contain and by adding the remaining five or six days of the current calendar month These average rates are of particular importance inasmuch as they show the relative cost to the bank of the various classes of deposits

This average rate figure is also useful in checking the accuracy of the interest computations This figure is obtained by comparing amounts arrived at in the computations with amounts running Rates of interest are fairly uniform for each class of deposits and investments, hence, the average figure can be interpreted in the light of the known prevailing rate and if it appears unreasonable, errors in calculation are indicated

The monthly interest earnings statement also shows the total average funds which the bank has employed in producing its income and in meeting its reserve requirement This figure consists of the bank's average investments in discounts, loans, stocks, and bonds, together with the average balance of invested funds in the foreign division, as shown in the preceding paragraphs, and the average amount of cash reserve maintained The average amount of cash reserve maintained consists of the daily average of cash kept in vault plus daily average balance maintained with the federal reserve bank

In addition, the average total funds on deposit during the month are shown. This figure is obtained by adding the total float and free balances to the total interest-bearing balances as shown on the statement The total float consists of items in process of collection upon which interest has not been paid Free balances are those depositors' balances upon which the bank pays no interest These are computed simply

THE NATIONAL CITY BANK OF NEW YORK

INTEREST EARNINGS STATEMENT FOR MONTH OF 192

	INTEREST	AV BALANCE	AV RATE	JANUARY 1 TO DATE		
				Interest	Av Balance	AV RATE
Interest Receivable						
Discounts						
Loans						
Foreign Department*						
Stock—Bonds .						
Cash Reserve .						
Total Interest and Avail able Funds .						
Interest Payable						
Domestic Banks						
Individuals						
Time Deposits .						
Foreign Banks						
Individuals						
Time Deposits						
Foreign Sundries						
Certificates of Deposit						
U S Government Deposits						
Trust Deposits						
Borrowed Money						
Borrowed Bonds						
Total Interest and Funds						
Float and Free Balances						
on Deposit						
Net Interest Earnings						
Commissions						
Transfers and Registrations						
Trust Department						
Coupon Paying						
Miscellaneous						
Exchange						
Rent						
Sundries						
Total Interest Earnings and Commissions						
Less Expenses						
Excess Interest Earnings and Commissions .						

\* The investments and the deposits of the foreign division are shown merely for statistical purposes in order to arrive at the total available funds and deposits of the bank. The interest figure given for foreign investments is an arbitrary one, exactly equal to interest payable on foreign deposits, the idea being simply to eliminate foreign interest from this statement.

Form 91 Monthly Interest Earnings Statement

by taking the difference between the average interest balances and the average actual balances

Form 91 shows the form of interest earnings statement used.

### **Consolidated Statement of Earnings**

To the domestic earnings are added the foreign earnings, the gross foreign earnings consist of the earnings of the traders (estimated for the purposes of this statement), interest, interest on excess deposits mentioned in the above paragraph, discount, commissions, and exchange. These items are largely self-explanatory. The interest consists principally of that earned on the foreign due from banks' accounts, on overdrafts, and interest earned in connection with commercial credits. Discount consists of that earned by the foreign discount department on dollar items. Commissions consist of those earned under commercial credits, travelers' checks and letters of credit, custodian fees, etc. From these gross earnings is deducted the interest paid on deposits. The result is the earnings of the home office. To obtain the total foreign profits the estimated profits of the branches are added. On account of the nature of foreign business, earnings do not remain fixed, they are subject to frequent adjustments, and do not lend themselves to the application of the principles of accrual in the same manner as domestic earnings. Because of this, all foreign earnings are computed on a cash or on an estimated basis.

From the total earnings of the bank, as obtained by adding the domestic and the foreign earnings together, the total expenses are deducted. These consist of salaries, taxes, and other expenses as obtained from the expense ledgers. The result is the net earnings figure. To the net earnings as obtained in this way are added losses recovered, while dividends paid and bond department write-offs are deducted.

THE NATIONAL CITY BANK OF NEW YORK  
CONSOLIDATED STATEMENT OF EARNINGS FOR MONTH OF  
192

	CURRENT YEAR		LAST YEAR
	Current Month	Jan 1 to Date	SAME PERIOD
Interest Receivable			
Interest Payable			
Net Interest Earnings			
Commissions			
Exchange			
Rent			
Sundries			
Bond Department Profits			
" " Losses			
Total Domestic Earnings			
Less Interest on Excess Foreign			
Deposits			
Domestic Earnings			
Foreign Department Profits			
Traders (Estimated)			
Interest			
Interest on Excess Deposits			
Discount			
Commissions			
U. S. Currency			
Foreign " "			
Commercial Credits Export			
Sundry			
Total			
Deduct Interest Paid on			
Deposits			
Foreign Department Profits			
Add Branches (Estimated)			
Total Foreign and Branch			
Profits			
TOTAL EARNINGS			
Deduct			
Salaries			
Taxes			
Other Expenses			
Total Expenses			
NET EARNINGS			
Net Earnings as Above			
Losses Recovered			
Bond Department's Write Ups			
Branch Profits			
Sundry			
Total Credits			
Dividends Paid			
Bond Department's Write Offs			
Sundry			
Total Debits			
Net Addition to Undivided Profits			
Undivided Profits at Beginning of			
Year			
Present Balance Undivided Profits			
AVERAGE RATE			
Earned on Capital, Surplus, Un			
divided Profits, and Deposits			

Form 92 Monthly Consolidated Statement of Earnings

Losses recovered consist of items previously charged off but which have since been collected Bond department write-offs consist of depreciation on bonds on account of falling markets The result is the net addition to undivided profits for the month under consideration

THE NATIONAL CITY BANK OF NEW YORK  
CONDENSED STATEMENT OF EARNINGS FOR MONTH OF  
192

	CURRENT MONTH	JAN 1 TO DATE
Domestic Earnings .		
Foreign Earnings*		
Total Income		
Less Expense		
Net Earnings		
Add Losses Recovered		
Bond Department's Write Offs .		
Branch Profits		
Sundries		
Deduct		
Dividends Paid		
Bond Department Write Offs		
Sundries		
Balance		
Undivided Profits Beginning of Year		
Present Balance Undivided Profits		

TOTAL AVERAGE DEPOSITS

Percentage to Total Average Deposits of	Percentage to Capital Stock of Net
Interest Paid	Earnings
Total Expenses	Percentage to Capital Stock Surplus
Net Earnings	and Undivided Profits of Net
	Earnings

Average Rate of Interest Received  
Average Rate of Interest Allowed on Deposits  
Average Rate Earned on Capital, Surplus, Undivided Profits,  
and Deposits

\* This does not include foreign exchange or bank profits



Certain other data of a statistical nature is included in the statement. The undivided profits at the beginning of the year are added to the net addition to undivided profits since that time to show the present balance of undivided profits, and deposits are shown—in other words the average rate earned on all funds of which the bank has full use. Form 92 shows the form of consolidated statement of monthly earnings.

### **Condensed Statement of Earnings**

For the ready reference of the officers a condensed statement of earnings is prepared from the consolidated statement. Form 93 shows the condensed statement of earnings.

### **Statement of Average Balances and Net Earnings by Districts**

In order that the results of the fiscal period in each official district of the bank may be shown, figures for the districts are combined as shown in Form 94.

### **Closing the Books**

The books of the banks are closed semiannually. At the time of closing, entries closing out the nominal accounts of the ledger and transferring the resultant balances into the Undivided Profits account are passed through the journal operated in connection with the voucher register. At this time discrepancies due to the method of estimating the profits of the traders and of the branches are corrected.

### **Weekly Statement to the Clearing House**

At the close of business on each Friday the bank is required under the constitution of the New York Clearing House Association to submit a statement showing the daily average figures and the actual figures on the date of the report, of certain essential items in its statement. These facts are derived from the daily statement book.

**THE NATIONAL CITY BANK OF NEW YORK**  
**STATEMENT OF AVERAGE BALANCES AND NET EARNINGS FOR**  
**FEDERAL RESERVE AND FOREIGN DISTRICTS**

	DOMESTIC DISTRICTS					FOREIGN DISTRICTS			
	1	2	3	4	5	1	2	3	4
Total Average Balances— this month									
Total Average Balances— last month									
Difference									
Earnings at % per									
Annual									
Expenses									
General									
Interest Paid									
Overhead at c per									
M on average deposits									
Total Expenses									
Net Profits for Month									
% of Total Expense to									
Earnings									
% of Net Profits for Month									
to Average Balances									
Average Rate of Interest									
Paid on Average Balances									
Actual Number of Accounts									
(Exclusive of Inactive									
Ledger)									
FOR MONTH									
Av Bal New Accounts									
Av Bal Accounts Closed									
No Accounts Opened									
No Accounts Closed									
TO DATE									
Av Bal New Accounts									
Av Bal Accounts Closed									
No Accounts Opened									
No Accounts Closed									

Form 94 Statement of Average Balances and Net Earnings by Districts

### Report to the Comptroller of the Currency

By law the Comptroller of the Currency is required to call upon national banks for a statement of condition at least five times a year. The correctness of the statement is attested to by the cashier or the president of the bank and by three directors. It is also sworn to before a notary public. A certain portion of the statement, which constitutes a complete balance sheet of the bank, is required to be pub-

PLEASE FOLD THIS SIDE OUT.

RESOURCES		Assets	Liabilities	Equity
1. Loans and discounts, including advances (except those shown in 2 and 3)				
2. Acceptances of other banks discounted				
3. Customers' liability amount of acceptances of this bank purchased or discounted by 1				
* Total loans (see schedule No. 2)				
4. Notes and bills represented by Fed. Res. Receipts (what bank acceptances sold) (see item 55 and schedule No. 2)				
5. Notes and bills represented by other Fed. Res. Receipts (what bank acceptances sold) (see item 55 and schedule No. 2)				
6. Acceptances of other banks payable at future date (what bank sold) (see item 55 and schedule No. 2)				
7. Foreign bills of exchange or drafts with indorsements of Gold Receipts, not shown under item 4, above (see item 55)				
8. Overdrafts, secured, & _____ (see schedule No. 17)				
9. Customers' liability on account of drafts paid under Letters of Credit, and for which this bank has not been reimbursed				
10. A. Customers' liability amount of "acceptances" secured by this bank, and for which this bank has not been reimbursed				
B. Liability of foreign banks and bankers for drafts and bills accepted by this bank to extend dollar exchange and new guaranties				
11. U. S. Government securities owned (see note):				
a. Deposited in secure depositories (U. S. bonds per value)				
b. Pledged to secure U. S. deposits (per value)				
c. Pledged to secure postal savings deposits (per value)				
d. Pledged as collateral for State or other deposits or bills payable				
e. Issued				
f. Owned and unpledged				
g. Premiums on U. S. bonds				
h. War Savings Certificates and United States Savings Bonds				
i. Deposited with State Authorities in accordance with provisions of Sec. 11-K, Federal Reserve Act				
j. Deposited with Trust Departments in accordance with provisions of Sec. 11 K, Federal Reserve Act				
Total U. S. Government securities				
12. Other bonds, securities, etc.				
a. Bonds (other than U. S. bonds) pledged to secure U. S. deposits				
b. Bonds (other than U. S. bonds) pledged to secure postal savings deposits				
c. Bonds and securities (other than U. S. securities) pledged as collateral for State or other deposits (see item 11, above)				
d. Bonds owned (other than U. S. bonds)				
e. Securities, other than U. S. bonds (not including stocks) owned and unpledged				
f. Government bonds and other bonds of corporations owned for not less than ONE YEAR nor more than THREE YEARS				
g. Deposited with State Authorities in accordance with provisions of Sec. 11 K, Federal Reserve Act				
h. Deposited with Trust Departments in accordance with provisions of Sec. 11 K, Federal Reserve Act				
Total bonds, securities etc., other than U. S. (see schedule No. 10)				
13. Stocks, other than Federal Reserve bank stock				
14. Stocks of Federal Reserve banks (50 per cent of subscriptions)				
15. A. Value of banking loans owned and non-reimbursed				
B. Details of banking loans owned and non-reimbursed				
16. Real estate and other things owned				
17. Assets owned with Federal Reserve bank				
18. Assets owned with Federal Reserve bank in process of collection (not available to reserve)				
19. Cash in vault and not available for use National banks (see schedule No. 3)				
20. Not accounts of other banks, branches, and trust companies in the United States (other than included in items 12, 13, 14, or 15)				
21. Exchange for clearing house				
22. Checks on other banks in the same city or town as reporting bank (other than item 14)				
Total of items 12, 13, 14, 15, 16 and 17				
23. Checks on banks located outside of city or town of reporting bank and other cash items (see schedule No. 1)				
24. Redemption fund with U. S. Treasurer and due from U. S. Treasurer				
25. Interest earned but not collected—on notes and bills receivable not paid due				
26. Other assets, if any (if space is not sufficient, attach schedule giving the nature and the amount of each item included herein)				

TOTAL (to avoid discrepancies the total should be verified)  
 (At) of the total loans and discounts shown above, the amount on which interest and discount were charged at rates in excess of the \_\_\_\_\_ per cent is \_\_\_\_\_

State of \_\_\_\_\_  
 County of \_\_\_\_\_  
 I, \_\_\_\_\_, sworn to and subscribed before me this \_\_\_\_\_ day of \_\_\_\_\_, 1920, and I hereby certify that I am not an officer or a director of this bank.

(1) CHECKS ON BANKS LOCATED OUTSIDE OF CITY OR TOWN OF REPORTING BANK, AND CASH ITEMS

a. Checks and drafts on Federal Reserve bank (if not in this city)				
b. Checks and drafts on banks outside of this city				
c. Interest Revenue charge				
d. Cash items				
Total (this amount must agree with item 14 of "Statement")				

(2) COUNTERPARTS OF REPORTS

a. Certificate of deposits issued in favor of other National banks and other institutions				
b. Certificate of deposits issued in favor of State banks and other non-National banks				

(3) CASH IN VAULT AND NET AMOUNTS DUE FROM NATIONAL BANKS

a. Gold coin				
b. Silver and minor coins				
c. Checking house certificates or other specific and other Federal Reserve (Sec. 1012)				
d. Paper currency				
Total cash				
Net amount due from National banks				
Grand total (this amount must agree with item 14)				

(4) Statement to the Comptroller of the Currency

NOTICE:

EVERY BLANK SPACE MUST BE FILLED IN WHERE THERE ARE NO FIGURES TO GO IN A PARTICULAR COLUMN THE WORD "NONE" MUST BE WRITTEN OR STAMPED THIS REGULATION WILL BE ENFORCED

(DO NOT ERASE OR CHANGE ANY OF THE PRINTED ITEMS)

TREASURY DEPARTMENT  
OFFICE OF THE COMPTROLLER OF THE CURRENCY  
WASHINGTON, D. C. 20548

LIABILITIES		DOLLARS	Cts.
21 Capital stock paid in			21
22 Surplus fund			22
23 a Undivided profits			23
b Less current expenses, interest and taxes paid			24
25 Interest and Discount collected or credited in advance of maturity and not earned—approximate			25
26 Amount reserved for taxes accrued			26
27 Amount reserved for all interest accrued			27
28 Overriding notes outstanding (see Schedule No. 6)			28
29 Amount due to Federal Reserve bank (national banks)			29
30 Net amounts due to National banks (see Footnote)			30
31 Net amounts due to banks, bankers and not members in the United States and foreign countries (other than banks) (see Footnote)			31
32 Certified checks outstanding			32
33 Cashier's checks on own bank outstanding			33
Total of Items 20 to 33 and 34			34
DEMAND DEPOSITS (other than bank deposits) SUBJECT TO RESERVE (deposits payable within 30 days):			
35 Individual deposits subject to check			35
36 Certificate of deposit due in less than 30 days (other than for money borrowed)			36
37 State county or other municipal deposits secured by pledge of assets of this bank			37
38 Deposits requiring notice, but less than 30 days			38
39 Dividends unpaid			39
40 Other demand deposits			40
Total of demand deposits (other than bank deposits) subject to Reserve, Items 34 to 40			41
TIME DEPOSITS SUBJECT TO RESERVE (payable after 30 days or subject to 30 days or more notice, and Period Savings):			
42 Certificate of deposit (other than for money borrowed)			42
43 State county or other municipal deposits secured by pledge of assets of this bank			43
44 Period savings deposits			44
45 Other time deposits			45
Total of time deposits subject to Reserve, Items 42 to 45			46
UNITED STATES DEPOSITS (other than Period Savings):			
47 a War Loan Deposit Account			47
b War Savings Certificate and Thrift Stamp Deposit Account			48
c Other United States deposits, including deposits of U. S. disbursing officers			49
d U. S. Government Securities borrowed without furnishing collateral security for same			50
e U. S. Government Securities borrowed for which collateral security was furnished			51
f Other bonds borrowed without furnishing collateral security for same			52
g Other bonds borrowed for which collateral security was furnished			53
h Securities (other than U. S. or other bonds) borrowed without furnishing collateral security for same			54
i Securities (other than U. S. or other bonds) borrowed for which collateral security was furnished			55
j Bills payable other than with Federal Reserve bank (including all obligations representing money borrowed other than rediscounts) (see Schedule No. 22 and 23)			56
k Bills payable with Federal Reserve bank (see Schedule No. 22 and 23)			57
58 State bank circulation outstanding			58
59 Letters of Credit and Travelers' Checks sold for and outstanding			59
60 a "Acceptances," executed by this bank for purchase (see Schedule No. 24)			60
b "Acceptances," executed by other banks for account and under guarantee of this bank (see Schedule No. 24)			61
c "Acceptances," executed to furnish dollar exchange			62
Total			63
d Less commissions of this bank purchased or discounted (see Item 17)			64
65 Time drafts of this bank outstanding			65
66 Time drafts of other banks sold (attach schedule giving the nature and the amount of each item listed on back)			66
67 Liabilities for rediscounts, with Federal Reserve bank (see Item 14 and schedule No. 25)			67
68 Liabilities for rediscounts other than with Federal Reserve bank (see Item 14 and schedule No. 25)			68
69 Acceptance of bills payable at future date, guaranteed by this bank by indorsement or otherwise (see Item 15)			69
70 Payable bills of exchange or drafts sold with indorsement of this bank, not shown under Item 4, above (see Item 16)			70
Total contingent liabilities (Items 59 to 70) (including Items 14, 15 and 16)			71
72 NET RES. ASSETS (Assets less liabilities less total b less total c less total d less total e less total f less total g less total h less total i less total j less total k less total l less total m less total n less total o less total p less total q less total r less total s less total t less total u less total v less total w less total x less total y less total z)			72

of the above-named bank, do solemnly swear that the above statement is true, and that the SCHEDULES or fully and correctly represent the true state of the several matters therein contained and set forth, to the best of

Correct—discrep: Cashier  
Director  
Director

DO NOT TO BE INCLUDED IN THE PUBLISHED STATEMENT

(4) NUMBER OF DEPOSIT ACCOUNTS

a Number of demand deposit accounts on which interest is allowed  
b Number of demand deposit accounts on which no interest is allowed  
c Number of time deposit accounts on which interest is allowed  
d Number of time deposit accounts on which no interest is allowed  
Total number deposit accounts

(5) RATES OF INTEREST ALLOWED OR PAID BY BANK

a On demand deposits (other than bank) over 12 months  
b On time deposits (other than bank) over 12 months  
c On deposits of other banks over 12 months  
d On notes and bills payable when last report is made  
e On bills payable when last report is made

(6) CIRCULATING NOTES

a Derived from Comptroller (not issued by other banks)  
b Less amount on hand and in Treasury for redemption  
c Outstanding (the amount of notes in circulation)  
(7) INTEREST RATES ON DEPOSITS AND OTHER MATTERS WHICH INTEREST ON DEPOSIT DID NOT RECORD IN LAST REPORT  
a Highest rate of interest charged on any time deposit (whether or interest, or non-interest, or demand)  
b Lowest rate charged on any time deposit (whether or interest, or non-interest, or demand)  
c Average rate of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
d Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
e Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
f Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
g Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
h Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
i Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
j Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
k Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
l Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
m Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
n Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
o Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
p Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
q Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
r Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
s Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
t Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
u Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
v Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
w Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
x Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
y Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)  
z Amount of interest charged on all time deposits (whether or interest, or non-interest, or demand)

**(8) LOANS AND DISCOUNTS.**  
(Including all Loans and Discounts on which Officers and Directors are Liable, and all Loans and Discounts Realized or Hypothecated for Little Payable.)

	Total Loan
a On demand paper with one or more individual or firm names (not secured by collateral).....	
b On demand secured by stocks and bonds to borrowers who keep deposit accounts with this bank.....	
c On demand secured by stocks and bonds to borrowers who do NOT keep deposit accounts with this bank.....	
d On demand, secured by other personal securities, including merchandise, warehouse receipts, etc.....	
e On time, paper with one or more individual or firm names (not secured by collateral).....	
f On time secured by stocks and bonds to borrowers who keep deposit accounts with this bank.....	
g On time, secured by stocks and bonds to borrowers who do NOT keep deposit accounts with this bank.....	
h On time, secured by other personal securities including merchandise, warehouse receipts, etc.....	
i Secured by real estate mortgages or other liens on realty NOT in accordance with Section 24 Federal Reserve Act, as amended.....	
j Secured by improved real estate under authority of Section 24 Federal Reserve Act as amended.....	
k Acceptances of other banks discounted.....	
l Acceptances of this bank purchased or discounted.....	
Total (this amount must agree with the total of Items 1a, 1b, and 1c. "Reserve").....	

**(9) LOANS SECURED BY WAREHOUSE RECEIPTS.**

a Amount of money loaned on the security of warehouse receipts or terminal receipts for coffee.....	
b Amount of money loaned on the security of warehouse or terminal receipts for wheat and other grain.....	
c Amount of loans secured by warehouse or terminal receipts for commodities other than coffee and grain.....	

**(10) OTHER PAPER.**

Notes owned outright for redemption with Federal Reserve Bank at date of this report, approximately.....	
<b>(11) BANK NOTES AND OVERDRAFT PAPER.</b>	
a Bank notes as defined in Section 5204, New Statutes.....	
b Other overdraft paper.....	
c Demand notes (not included in "a" or "b") held without demand or discounted for more than one year.....	

**(12) RED CROSS DEPOSITS.**

Amount on deposit, this date, for American National Red Cross, Red Cross War Fund, Red Cross Chapter, and other subdivisions.....	Number of accounts	Total
Amount to which the deposit accounts stand on books of this Bank (which make up the above total) and amount in credit of each account.....		Deposits balance date of this report.....
(Include interest, if none is due/owed)		

**(13) SUBSCRIPTIONS TO AMERICAN NATIONAL RED CROSS**

Total amount contributed by this bank to the American National Red Cross since passage of Act of May 21, 1918, authorizing such subscriptions.....			
<b>(14) LOANS EXCEEDING THE LIMIT Prescribed by Section 5102 of the Revised Statutes, including balances due from nonmember banks, exceeding the limit prescribed by Section 16 of the Federal Reserve Act. Overdrafts, if any, must be classed with Loans.</b>			
Name of borrower	How full received at bank	Name of bank	Enter full amount of loan.

**(15) LOANS TO OTHER BANKS AND TRUST COMPANIES.**

	National Banks	Other Member Banks	Nonmember Banks	Total
1. Amount loaned on U. S. War obligations (Liberty Loan Bonds, Victory Notes, and U. S. Certificates of Liquidation).....				
a On bills payable and redemptions.....				
b On Certificates of deposit.....				
2. All other loans (secured or unsecured).....				
a On bills payable and redemptions.....				
b On Certificates of deposit.....				
Total.....				

**(16) SECURITIES LOANED**

a U. S. Government Securities owned by bank and loaned to others (see footnote).....	
b Other bonds owned by bank and loaned to others.....	
c U. S. Government Securities borrowed by bank and loaned to others (see footnote).....	
d Other bonds borrowed by bank and loaned to others.....	

**(17) BONDS, SECURITIES ETC. (OTHER THAN U. S. SECURITIES)**

(Bonds, Claims, Judgments, and similar items should be included under this head)	
1 Domestic Securities:	
a State, county or other municipal bonds.....	
b Railroad bonds.....	
c Other public service corporation bonds.....	
d All other bonds.....	
e Claims, warrants, etc.....	
f Judgments.....	
g Collateral trust and other corporation notes.....	
2 Foreign government bonds:	
(1) Bonds of the German or Austrian Governments.....	
(2) Bonds of the Russian Government.....	
(3) Bonds of other foreign Governments.....	
b Other foreign bonds and securities.....	

**(17) OVERDRAFTS.**

	Secured	Unsecured
a Running over 6 months.....		
b Temporary.....		
c Overdrafts resulting from deposits being checked and charged to accounts (banks not allowed to properly check and charge to each).....		
Total (this amount must agree with Item 6, "Reserve").....		

<b>(18) LOANS MADE THROUGH CORRESPONDENT BANKS IN CENTRAL RESERVE CITIES ON DATE OF THIS REPORT</b>	
Total amount of money which this bank is loaning through its correspondent banks in New York City.....	
Total amount of money which this bank is loaning through its correspondent banks in other central reserve cities (Chicago and St. Louis).....	
Total (this amount must agree with Item 6, "Reserve").....	

1 Includes Liberty Loan Bonds, Victory Notes, Certificates of Liquidation, and all other issues of Government Securities.

NOTE. ALL SCHEDULES within or spanning in the word "Wine" where no amount is to be entered.

[illegible]

(28) LIABILITIES OF OFFICERS AND DIRECTORS, ANNUAL SALARIES, AND SHARES OWNED.									
1 (See note.) Names of officers and directors.	2 Office title.	3 Salaries for 1914 for 1915 for 1916 for 1917 for 1918 for 1919 for 1920 for 1921 for 1922 for 1923 for 1924 for 1925 for 1926 for 1927 for 1928 for 1929 for 1930 for 1931 for 1932 for 1933 for 1934 for 1935 for 1936 for 1937 for 1938 for 1939 for 1940 for 1941 for 1942 for 1943 for 1944 for 1945 for 1946 for 1947 for 1948 for 1949 for 1950 for 1951 for 1952 for 1953 for 1954 for 1955 for 1956 for 1957 for 1958 for 1959 for 1960 for 1961 for 1962 for 1963 for 1964 for 1965 for 1966 for 1967 for 1968 for 1969 for 1970 for 1971 for 1972 for 1973 for 1974 for 1975 for 1976 for 1977 for 1978 for 1979 for 1980 for 1981 for 1982 for 1983 for 1984 for 1985 for 1986 for 1987 for 1988 for 1989 for 1990 for 1991 for 1992 for 1993 for 1994 for 1995 for 1996 for 1997 for 1998 for 1999 for 2000 for 2001 for 2002 for 2003 for 2004 for 2005 for 2006 for 2007 for 2008 for 2009 for 2010 for 2011 for 2012 for 2013 for 2014 for 2015 for 2016 for 2017 for 2018 for 2019 for 2020 for 2021 for 2022 for 2023 for 2024 for 2025 for 2026 for 2027 for 2028 for 2029 for 2030 for 2031 for 2032 for 2033 for 2034 for 2035 for 2036 for 2037 for 2038 for 2039 for 2040 for 2041 for 2042 for 2043 for 2044 for 2045 for 2046 for 2047 for 2048 for 2049 for 2050 for 2051 for 2052 for 2053 for 2054 for 2055 for 2056 for 2057 for 2058 for 2059 for 2060 for 2061 for 2062 for 2063 for 2064 for 2065 for 2066 for 2067 for 2068 for 2069 for 2070 for 2071 for 2072 for 2073 for 2074 for 2075 for 2076 for 2077 for 2078 for 2079 for 2080 for 2081 for 2082 for 2083 for 2084 for 2085 for 2086 for 2087 for 2088 for 2089 for 2090 for 2091 for 2092 for 2093 for 2094 for 2095 for 2096 for 2097 for 2098 for 2099 for 2100 for 2101 for 2102 for 2103 for 2104 for 2105 for 2106 for 2107 for 2108 for 2109 for 2110 for 2111 for 2112 for 2113 for 2114 for 2115 for 2116 for 2117 for 2118 for 2119 for 2120 for 2121 for 2122 for 2123 for 2124 for 2125 for 2126 for 2127 for 2128 for 2129 for 2130 for 2131 for 2132 for 2133 for 2134 for 2135 for 2136 for 2137 for 2138 for 2139 for 2140 for 2141 for 2142 for 2143 for 2144 for 2145 for 2146 for 2147 for 2148 for 2149 for 2150 for 2151 for 2152 for 2153 for 2154 for 2155 for 2156 for 2157 for 2158 for 2159 for 2160 for 2161 for 2162 for 2163 for 2164 for 2165 for 2166 for 2167 for 2168 for 2169 for 2170 for 2171 for 2172 for 2173 for 2174 for 2175 for 2176 for 2177 for 2178 for 2179 for 2180 for 2181 for 2182 for 2183 for 2184 for 2185 for 2186 for 2187 for 2188 for 2189 for 2190 for 2191 for 2192 for 2193 for 2194 for 2195 for 2196 for 2197 for 2198 for 2199 for 2200 for 2201 for 2202 for 2203 for 2204 for 2205 for 2206 for 2207 for 2208 for 2209 for 2210 for 2211 for 2212 for 2213 for 2214 for 2215 for 2216 for 2217 for 2218 for 2219 for 2220 for 2221 for 2222 for 2223 for 2224 for 2225 for 2226 for 2227 for 2228 for 2229 for 2230 for 2231 for 2232 for 2233 for 2234 for 2235 for 2236 for 2237 for 2238 for 2239 for 2240 for 2241 for 2242 for 2243 for 2244 for 2245 for 2246 for 2247 for 2248 for 2249 for 2250 for 2251 for 2252 for 2253 for 2254 for 2255 for 2256 for 2257 for 2258 for 2259 for 2260 for 2261 for 2262 for 2263 for 2264 for 2265 for 2266 for 2267 for 2268 for 2269 for 2270 for 2271 for 2272 for 2273 for 2274 for 2275 for 2276 for 2277 for 2278 for 2279 for 2280 for 2281 for 2282 for 2283 for 2284 for 2285 for 2286 for 2287 for 2288 for 2289 for 2290 for 2291 for 2292 for 2293 for 2294 for 2295 for 2296 for 2297 for 2298 for 2299 for 2300 for 2301 for 2302 for 2303 for 2304 for 2305 for 2306 for 2307 for 2308 for 2309 for 2310 for 2311 for 2312 for 2313 for 2314 for 2315 for 2316 for 2317 for 2318 for 2319 for 2320 for 2321 for 2322 for 2323 for 2324 for 2325 for 2326 for 2327 for 2328 for 2329 for 2330 for 2331 for 2332 for 2333 for 2334 for 2335 for 2336 for 2337 for 2338 for 2339 for 2340 for 2341 for 2342 for 2343 for 2344 for 2345 for 2346 for 2347 for 2348 for 2349 for 2350 for 2351 for 2352 for 2353 for 2354 for 2355 for 2356 for 2357 for 2358 for 2359 for 2360 for 2361 for 2362 for 2363 for 2364 for 2365 for 2366 for 2367 for 2368 for 2369 for 2370 for 2371 for 2372 for 2373 for 2374 for 2375 for 2376 for 2377 for 2378 for 2379 for 2380 for 2381 for 2382 for 2383 for 2384 for 2385 for 2386 for 2387 for 2388 for 2389 for 2390 for 2391 for 2392 for 2393 for 2394 for 2395 for 2396 for 2397 for 2398 for 2399 for 2400 for 2401 for 2402 for 2403 for 2404 for 2405 for 2406 for 2407 for 2408 for 2409 for 2410 for 2411 for 2412 for 2413 for							

2) should indicate how the much needed support by citizens or other officials, give the correct amount in this column as indicated from column of disbursements. All columns must be same place. Whether officers or disburse are indicated in hand of you.

August 31 1920 both inclusive)

[illegible]

(30) AVERAGE BORROWINGS AND REDISCOUNTS WITH FEDERAL RESERVE BANK BY MONTHS.

Average aggregate amount which this bank was borrowing during each month, January 1, 1920, to August 31, 1920, from the Federal Reserve Bank of its district through member banks and Bill Treasuries:

January, 1920.	February 1920	March 1920.	April, 1920.	May 1920.	June, 1920.	July 1920.	August, 1920.
\$	\$	\$	\$	\$	\$	\$	\$

**ILLUSTRATION:** If a bank on January 1 should rediscunt with the Federal Reserve Bank commercial paper having ninety days to run, for \$50,000 and on March 16 should borrow for example \$50,000 on United States Bonds by Bill Payable from its Reserve Bank the bank's report here should show average aggregate rediscounts and bills payable in January \$50,000, for February \$50,000, for March \$75,000.

THE NATIONAL CITY BANK OF NEW YORK AND BRANCHES  
CONDENSED STATEMENT OF CONDITION AS OF MAY 4, 1920

*Assets*

Cash on Hand, in Federal Reserve Bank and due from Banks and Bankers and United States Treasurer . . . . .	\$254,008,322 18	
Acceptances of other banks . . . . .	26,934,110 29	
United States Treasury Certificates . . . . .	22,813,500 00	\$ 303,755,932 47
Loans and Discounts . . . . .	\$586,088,579 98	
United States Bond and other Bonds and Securities . . . . .	40,079,590 07	
Stock in Federal Reserve Bank . . . . .	1,800,000 00	627,968,170 05
Banking House . . . . .	5,000,000 00	
Due from Branches . . . . .	20,470,001 51	
Customers' Liability Account of Acceptances . . . . .	66,068,490 77	
Other Assets . . . . .	4,323,191.73	
		<u>\$1,027,585,786 53</u>

*Liabilities*

Capital, Surplus, and Undivided Profits . . . . .	\$ 84,855,526 65	
Deposits . . . . .	720,598,397 99	
Reserved for Taxes and Interest Accrued . . . . .	4,846,508 31	
Unearned Discount . . . . .	2,902,600 02	
Circulation . . . . .	1,399,930 00	
Due to Federal Reserve Bank . . . . .	106,460,066 76	
Other Bank Acceptances and Foreign Bills Sold with our Indorsement . . . . .	31,753,200 11	
Acceptances, Cash Letters of Credit, and Travelers' Checks . . . . .	68,143,630 51	
Bonds Borrowed . . . . .	3,333,200 00	
Other Liabilities . . . . .	3,292,726 18	
		<u>\$1,027,585,786 53</u>

lished in a local newspaper by the bank and notice of compliance of this requirement sent to the Comptroller

The information contained in this statement issued by the Comptroller to assure himself that the bank is complying with the law, hence the calls are made at irregular intervals for a statement as of a day just passed and without previous notice being given. The bank has only a limited time to comply with the Comptroller's call, hence the whole system of accounting is patterned to furnish the information required by the Comptroller easily and quickly. Because of its bearing on the accounting system the form of the statement is reproduced in full in Form 95

### **Published Statements**

While a bank's statement of condition is published at the time of the Comptroller's call, it is often issued for advertising purposes and for the information of customers.

In preparing the statement for publication for this purpose it is the common practice to rearrange it into a condensed and more readily understandable form, and one which at the same time brings out elements of strength in the bank's condition more clearly. Form 96 shows the published statement of the bank on the practices of which this book is written



## CHAPTER XXIV

### AUDITING

#### Internal and External Audits

In the chapters just preceding it has been shown that both the operating and the accounting procedure of the bank abounds in checks and controls designed to insure the accuracy of the records. Effective as these automatic controls are, they are not deemed sufficient for a large banking institution. They are accordingly supplemented by the activities of an experienced group of auditors who are constantly making tests to determine the accuracy of the work of the operating departments. In addition to these audits carried on by the auditing department, examinations are made by the government, the clearing house, and by the directors of the bank. The former may be spoken of as the "internal," and the latter as the "external" audits.

#### THE INTERNAL AUDIT

##### Auditing Work

The bank's own auditing activities are as follows:

1. The daily audits of certain current transactions
2. Reconcilements of the records of the bank with those of its customers
3. General audits, consisting of periodic examinations of the bank by departments
4. Branch bank accounting

The organization of the bank for the work of auditing consists of an auditing division under the control of an auditor responsible to the comptroller of the bank. The auditing division

is subdivided into four major departments: accounting, reconcilements, general auditors, and branch bank accounting. The accounting department has the function of making daily audits of current transactions. It also keeps the expense records of the bank, as was indicated in the preceding chapter. The reconcilements department attends to reconciling the bank's records with those of its depositors, the federal reserve bank, and foreign banks with which the bank keeps accounts. The function of the branch bank accounting department is to maintain accounting connections with the branches of the bank. The general auditors are a staff of examiners who make periodic audits of the various departments of the institution. In addition to these departments there is a staff of branch bank inspectors who make examinations of the bank's branches in much the same way as government examiners do in connection with domestic banks. These examiners are responsible to the comptroller of the bank direct, instead of to the auditor. Connected with the auditing division there is also a record filing department which files cash letters, collection ledgers, journal tickets, mail advices, paid cashier's checks, and all other records from the different departments of the bank from which entries to the accounts are built up. In this department are also filed reconcilements of customers' accounts and letters received from bank examiners and certified accountants requesting special statements or verification of balances.

## 1 The Daily Audit

Because of the effectiveness of automatic checks and controls it is not necessary to subject the operations of all departments to a daily audit. In the first place the system of proving and recording the work of many departments acts as an effective check over inaccuracies. As an example the receiving teller's department may be considered. The daily proof of this department shows that the total of the deposit slips sorted

according to customers ledgers equals the receipts of cash and cash items sorted according to the disposition made of them. The receiving teller holds over no work from one day to the next and those departments which receive work from him must verify the accuracy of his sendings in preparing their own proofs

In the second place the records of some of the departments are built up in duplicate by another department, and the records of the one act as an effective control over those of the other. A very good illustration of this is the system whereby the work of the deposit ledger bookkeepers is exactly paralleled by the work of the statement clerks and further controlled by the general bookkeepers, each of whom builds up his records in so far as is practicable from separate sources. In certain other departments which are not surrounded by automatic controls the nature of the work may be such that the results of the daily audit are checked by agencies outside the bank. Thus the collection departments account directly to customers for proceeds of collections, and the assumption is that these customers will report any chance errors which may occur.

### **Continuous Audits**

Whenever an operation is such that it is not automatically checked by one of these methods, a daily audit is used. A daily audit consists in reviewing or checking the actual transactions immediately after they have passed through the operating departments. These daily audits are of two kinds: the continuous audit, and the spot audit. Certain transactions, such as issuing credit instruments, travelers' checks, certificates of deposit, cashier's checks, etc., receiving negotiable funds not accounted for on cash proofs, making adjustments with customers, computing earnings, making outlays, etc., require the closest supervision at all times regardless of the efficiency of

the departments which handle them. All transactions of this sort are accordingly checked immediately by the accounting department.

Daily audits are also used for other purposes. Occasionally a test audit made by the general auditors may indicate a low degree of efficiency in the operating personnel of a department. Again, reorganizations and radical changes in the system of doing things in a department may be made. In either case daily audits of each transaction passing through the department are likely to be used until it is ascertained that the efficiency of the department has been restored or that the new system is working successfully.

### Spot Audits

In general, however, the spot audit, which is merely a temporary form of daily audit, is used in place of the continuous audit wherever practicable. In making this type of audit the auditors make their appearance in a department at irregular intervals and check all the work passing through a specific process for a few days until they have a good idea of how the work is being done. Aside from the element of cost involved, the continuous audit is undesirable in that realization of the fact that their work is being constantly checked tends to lessen the degree of alertness which the clerks exercise. On the other hand, knowledge of the fact that the auditors of the bank may appear for the purpose of making a spot audit at any time has the effect of increasing operating efficiency.

To maintain the efficiency of the auditing staff itself, a certain degree of isolation from the other departments of the bank is of advantage. This purpose is accomplished by transferring the auditors from one type of work to another at frequent intervals. This device also serves the purpose of checking the work of each member of the auditing department,

since it is fall to assume that each auditor who is assigned to a new task should accomplish about the same results as his predecessor.

In a work of this sort it is impracticable to give each daily audit made. The audits involve an examination at one time or another of a large number of the operating departments. The work consists mainly in checking the actual transactions each of which is described in detail in preceding pages. No particular purpose would be served in describing them again. Furthermore in the case of the spot audit there is no fixed program covering the procedure. Rather, spot audits of varying intensity are made here and there as necessity demands.

In the following pages therefore only a few of the continuous audits will be described in order to give the reader an idea of the nature of the work done.

### **Audits of Issuance of Credit Instruments**

Among the transactions subjected to a continuous audit are those involving the issuance of credit instruments and similar items, such as cashier's checks, certificates of deposit, certified checks, domestic and foreign drafts, travelers' checks and letters of credits, commercial credits, and cable and telegraphic transfers. The work of auditing the issuance of cashier's checks may be taken as an example. In auditing these the auditors are concerned first with protecting the bank against unauthorized issues, and second with determining that transactions which have been authorized are entered correctly on the books of the bank.

### **Number Control System**

Protection against the unauthorized issues of cashier's checks is secured through the use of a number control system. Under this arrangement all blank checks are numbered serially and kept in the possession of the auditing department. The

operating departments are permitted to keep on hand only a small supply sufficient for daily requirements. To make it possible to identify each check readily a distinctive letter or symbol indicating the department of issue is affixed to the serial number. Record of blank forms in the hands of the departments is kept by means of number sheets each of which lists the numbers of the blanks held by a particular department. As the instruments are issued stubs bearing the corresponding numbers and the authority of an officer to issue them pass through the accounting department where the numbers are crossed off the number sheet. By this method each department is held strictly to account for all its blank instruments either in the form of a stub giving details of the transaction, if the instrument has been issued, or in the form of the canceled instrument itself, if for some reason it was prepared in error.

Cashier's checks are audited both for the purpose of determining that the entries made by the issuing department are correct and also that the Cashier's Check account kept by the general bookkeepers is accurate. Auditors regularly attached to departments issuing cashier's checks obtain stubs from the checks as the officers sign them. The stubs, which contain details of how the transaction was handled, are compared with the original entry material for the transactions which give rise to them in order to determine that the bookkeeping tickets made in connection therewith have been correctly prepared.

Control over the Cashier's Check account of the general bookkeeper's department is maintained by means of a proof kept by the auditors. This proof is virtually a second control account for cashier's checks. On the credit side checks issued are entered according to the stubs received by the accounting department each day. When the checks are paid and debited to the General Bookkeeper's Control account the canceled

checks are passed to the accounting department where they are entered on the debit side of the proof, attached to the corresponding stubs, and filed. The balance of the proof shows cashier's checks outstanding and should agree with the Cashier's Check account on the general books.

The accounting department also has the stub representing each check outstanding. At intervals these are compared with the Cashier's Check account.

### **Auditing Shipments of Valuables**

Shipments of money, securities, and other valuables are subjected to continuous audits to determine that they are made in conformity with instructions, that they are addressed to the proper consignees, and that the bank receives an authentic acknowledgment from the consignee stating that he received the shipment.

In auditing shipments of gold or other money, the instructions ordering the shipments are used as a basis for the audit. The instructions are authenticated by having either the signatures or the test words verified. Then to make sure that no details were omitted they are compared with the affidavit made out by those who despatched the shipment. Finally they are checked against the auditor's copy of the advice of debit sent to the consignee and against the entry in the ledger. The copy of the debit advice is held for the purpose of following up the shipment if need arises. When the acknowledgment of arrival of the shipments is received it is compared with the advice to make sure the sending arrived intact.

Shipments sent out by the outgoing registered mail department are recorded in a shipment book. Each is accompanied by a card which is to be signed and returned as an acknowledgment of receipt of the shipment by the consignee. At the return of these cards the signatures upon them are compared with the names appearing in the shipment book to make sure

that the sendings reached the proper parties. All cards remaining outstanding beyond the regular transit time are made the subject of a special investigation by the auditor who with the co-operation of the postal authorities endeavors to account for the missing shipment.

### **Correction Entries**

Complete control over entries correcting work which has already been entered in the books of the bank is centralized in the accounting department. Whenever an error is located a correcting entry is made by means of a ticket of distinctive color. A detailed record of all errors located by the auditors is kept by the accounting department. Once each month a list is prepared showing the departments making errors and the number and kind made by each department. This list is forwarded to the cashier and is used as a guide in determining the efficiency of the various departments.

### **2. Reconciliation of Accounts**

A very effective check over the accuracy of the depositors' ledgers, the "due from foreign banks" accounts, and the Lawful Reserve account is provided in the periodical reconciliation of accounts.

While the work of reconciling the accounts of domestic and foreign depositors is performed by separate units, no distinction will be made between the two, for the processes are quite similar. The statement of account sent out by the bank is, of course, the medium through which reconciliation is effected. It lists in detail every debit and every credit which has been passed to an account during a given month. Along with this statement the customer receives the canceled vouchers and a reconciliation blank, and he is requested to make a careful comparison with his own records. If both versions of the account agree he records the balance upon the recon-



clement blank, signs it, and returns it to the bank; if they do not conform he enumerates the discrepancies. When the reconciliation forms return to the bank the signatures are verified before the reports are accepted. Those returns which constitute approval are again checked with the balances shown on the books as of the proper date, while those which have exceptions noted upon them are subjected to thorough investigations. Each discrepancy is treated separately and the findings of the investigation are reported to the customer. If the bank is in error the proper correction entry is made. In case the customer made the error the matter is explained to him in detail and he is requested to bring his records into agreement with those of the bank.

The farther behind current transactions the reconcilements fall, the more difficult it is to reconcile accounts. Hence every effort is made by the bank to have reconcilements made regularly and promptly. All reconcilements which remain outstanding are closely followed up. If ordinary letters of reminder do not bring a response from the customer a letter is written to someone in authority requesting that he give personal attention to the matter.

### **Reconciliation of Due from Foreign Banks Accounts**

In the reconciliation of its foreign "due from banks" and its lawful reserve accounts, the position of the bank is the reverse of that outlined above. As a depositor in banks abroad and with the federal reserve bank, it in turn receives statements of account current and is requested to compare them with its own records. The federal reserve bank sends a statement of account each day. This is reconciled promptly after it is received. Foreign banks send statements monthly as a general rule. Each discrepancy is thoroughly investigated and a permanent record is made of it before it is reported to the foreign bank. Thereafter both banks work upon the prob-

lem until their various records are found to be in conformity

A common point of disagreement in the foreign account is that of value dating. The New York bank frequently discovers that a transfer which it has purchased, value date as of a certain day, was credited to its account on some other day. Many of the errors of this sort are discovered by the bookkeepers by means of advices sent in by foreign banks whenever they credit the account of the American bank. Others, however, are not located until the reconciliation is made. Such errors as these result in a loss of interest to the bank if its account abroad is credited at a later date than that which was made the basis of its transaction with the purchase of the transfer. In such a case the purchaser is communicated with and reimbursement obtained. Conversely, if the bank obtains earlier credit abroad than it expected, it has overcharged the purchaser and the excess interest is returned to him.

### **Reports Concerning Customers' Relations**

Whenever a bank examiner or a public accountant makes a survey of the affairs of a client of the bank, he sends a report form to the bank requesting it to supply certain data concerning its relations with the customer. Before answering an inquiry of this sort the bank takes every precaution against giving information to unauthorized persons. An inquiry from an authorized bank examiner is complied with by sending the information direct, but in other cases the bank obtains the customer's orders in the matter before the information is delivered to the applicant. Oftentimes when inquiry unaccompanied by the signed request of the depositor comes in from a public accountant, the bank sends the information called for to the depositor, requesting him to deliver it to the accountant if he wishes to authorize compliance with the request.

In answering such an inquiry the blank form submitted

by the one who desires the information is circulated among the various departments of the bank, each one noting thereon the relations which it has had with the subject. In addition to this report a photograph of the statement of account current is forwarded to the one making inquiry.

### 3. General Audit

The general audit in the bank is in many respects similar to the audits made by the outside agencies. In the continuous and the spot audit the procedure is to submit some specific banking process to detailed examination while the work is in process. The general audit, on the other hand, consists of a comprehensive examination of the records covering the operations, generally of a specific department, over a considerable period of time. The movements of the auditors from department to department are guarded with the greatest secrecy, as are those of a national bank examiner from bank to bank, the inspection is made with the same critical attitude and the object is a similar one, namely, that of verifying the assets, liabilities, profits, and losses of the bank as expressed in the daily statement or balance sheet. Incidentally the general audit protects the bank against fraud from within or without, and it serves to indicate faults in the operating procedure.

The scope of the general audit includes not only those departments which are not subjected to daily and spot audits, but also those which are constantly audited. The audits, however, are restricted in the main to those phases of the bank's work which have to do with handling money, securities, etc.

It is the aim of the auditors to inspect each department several times a year, special audits being made as they are deemed expedient. The routine of these audits is necessarily secret, especially so to those departments which are subject to the audit. Were secrecy not necessary, however, it would

be practically impossible to give details of the general audit in a work of this sort because the procedure in the various departments differs with the nature of the work transacted in those departments.

In entering a department the general auditors take possession of all cash, securities, and other valuables held. In order that the department may not be hampered in its work, additional items are received or given out upon the permission of the auditors who, however, keep their own independent record of such transactions. In order that records which are constantly needed by the department under investigation may be available both for the department and for the auditors, photographic copies of them are made.

Each account involving the inventory of some valuable commodity, such as cash, securities, notes, etc., is verified by actual count. Wherever possible the assets and liabilities of the bank, as well as securities held for others, are verified from independent sources. In examining the collateral for a loan, for example, reconcilements of the bank's records with those of the borrower are made directly with the borrowers by the auditors. Customers' deposit balances, securities held for customers, and other items of this sort are likewise verified by writing to the customers direct.

### **Reports on the Findings of the Audit**

Upon the completion of an examination a report is prepared on the condition of the department for the use of the executive managers and the comptroller of the bank. Copies of such reports are kept on file for guidance in future examinations.

### **Improvements in Accounting System**

Equal in importance to verifying the accuracy of the bank's record is the function exercised by the general auditors in

making studies of accounting methods, departmental routine, etc., with a view to improving them. Improvements in system or routine may originate with the general auditors or elsewhere, whenever they originate, however, they are submitted to the auditing staff for criticism and approval from the accounting standpoint before they are adopted.

### **Branch Bank Auditing**

The work of auditing the affairs of the foreign branches of the bank is performed by two separate organizations—the branch bank accounting department, and the branch bank inspectors. The former is permanently attached to the home office and its work consists of preparing statements and statistics of the branches. The latter force is a group of traveling auditors who go from one branch to another making inspections similar to the ones conducted by the general auditors.

In accordance with the laws under which national banks operate the financial accounts of each branch are kept separate from those of the home office. To keep check on the affairs of the branches, however, the home office requires periodic statements of conditions. Each branch is required to send a weekly statement of its condition by cable. Uniform accounting methods and standard records used by the branches make them miniatures of the home office. By means of a specially devised code system the weekly statements of the branches may be sent in only a very few words. When they are received these statements are combined with the statement of condition of the home office in order to show the condition of the institution as a whole. The statement of each branch is also submitted for analysis and inspection to the administrative group in charge of the territory of the branch.

A more elaborate statement is sent by mail by each branch at the close of the month. The monthly statement serves as a check upon the cable reports and gives the position of the

bank in detail with respect to loans, discounts, overdrafts, past due bills, due from banks, expenses, interest receipts, disbursements, etc. In addition to these, special reports are required whenever the foreign branch has exceeded its allotment in the purchase or sale of foreign exchange, and whenever its holdings of government paper, municipal bonds, etc., in the form of investments or collateral fluctuate beyond certain limits. When the Comptroller of the Currency issues a call for the statement of condition of a national bank, he requires a statement from each foreign branch of that bank as well. The branches are notified of such calls by cable and report their detailed condition by mail to the branch bank accounting department for submission to the government. Semiannually the profits of the branches are transferred to the balance sheet of the home office. At this time elaborate reports are submitted by each branch.

### **Branch Bank Inspection**

The branch bank inspection work consists of regular audits or examinations of each branch made by a group of auditors representing the home office. At irregular intervals—in all, four times a year—these inspectors take charge of a branch bank and make a searching investigation into all of its affairs. The inspection consists, of course, in counting the cash and securities, verifying the loans and discounts, and reconciling the records of the branch with those of its customers and the home office, etc. In addition, however, the investigation aims to ascertain the quality of the investments which the branch has made. This is done by making a regular credit investigation of the borrowers wherever possible and by studying the economic and political conditions of the community. A large amount of valuable information is incidentally obtained for the credit files of the bank. The findings of the examination are submitted in detail to the officer in charge of the territory.

## THE EXTERNAL AUDIT

The internal audits just described are initiated by the bank to assure itself that the records are exact. As a further assurance to the public, to other banking institutions, and to the stockholders, that the affairs of the bank are being managed conservatively and efficiently the bank is subjected to audits from the following external agencies:

- 1 National bank examiners
2. State bank examiners
- 3 The clearing house
- 4 A committee of the board of directors of the bank

**Audits by National Bank Examiners**

In the United States it is considered that the connection of the public at large with banks as depositors demands that the government protect their interest by close supervision over the affairs of each bank. In keeping with this doctrine each class of bank is limited in its activities by law and a rigid system of reports and inspection is maintained. The Federal Reserve Act requires that the Comptroller of the Currency appoint examiners to investigate the affairs of each member bank at least twice a year and it empowers the examiners to make a thorough inspection of all the affairs of the bank and to examine any of the officers and agents under oath. These audits are designed not only to verify the bank's statement of condition which is submitted five times a year, or oftener, to the Comptroller, but also to determine that the law regulating national banks is being strictly observed and that the bank is being conservatively managed.

Upon the recommendation of national bank examiners a bank may be thrown into liquidation by the Comptroller of the Currency, in keeping with the responsibility reposed in the examiners, therefore, the national bank examination is

a most far-reaching one. The examiner with his staff of auditors appears at the bank without having given notice of his intention and he takes complete charge of its affairs much as the general auditors take charge of a particular department. The national bank examiner is particularly interested in ascertaining that the law limiting the amount which can be loaned to any one borrower to 10 per cent of the capital and surplus of the bank, the provision setting up a reserve requirement of 13 per cent and 3 per cent against net demand and time deposits, respectively, and the law limiting the circumstances under which a bank may accept drafts and the amount which it can accept, are being complied with. Accordingly the bank's Lawful Reserve account is checked back for a period of 30 days. Lists showing the total amount loaned to each borrower are also compiled from the various departments making loans, such as loans, discounts, commercial credits, etc. Acceptances arising from commercial credits are checked up from the records of the commercial credit departments.

In determining the conservatism of the management of the bank the examiners confine themselves largely to a consideration of the kinds of loans and investments that are being made. In this connection they consider both the liquidity and the security of the investments, the aim being to establish the fact that the bank is carrying on a strictly commercial business. Each loan is examined for adequacy of collateral in the light of existing market prices. In examining discounts and commercial credits, the credit rating of the borrower is considered in so far as it is possible. The activities of the foreign exchange traders are thoroughly investigated in order to establish that the practices of the bank in this respect are conservative.

The examination of other assets and liabilities of the bank follows about the same course as that pursued by the general auditors. For example, cash and securities accounts are veri-



fied by taking actual inventory To make sure that cash items, such as checks, drafts, etc., in the hands of the transit and city collection departments are bona fide instruments the examiner encloses a notice in the outgoing letter to collecting agents requesting them to notify him of the results of the collection process Each account of the bank is reconciled Domestic accounts are reconciled directly as between the examiner and the depositors, while foreign accounts, because of the time which would be required for direct reconcilements, are verified by means of a detailed examination into the records of the bank's own reconciliation department Certificates of deposit, cashier's checks, and certified checks are audited by checking the canceled instruments against the original entries and proving the open entries against the totals on the general ledger

The results of the audit are embodied in a detailed report which is submitted to the Comptroller of the Currency The Comptroller then informs the directors of the bank of the results of the audit and points out any changes which appear desirable from his point of view

### Clearing House Examinations

The clearing house association maintains a staff of examiners, who at least once a year inspect each clearing house bank and also those banks which clear through members of the association This inspection aims particularly to establish that the bank is in sound financial condition It consists therefore largely in taking an inventory of the bank's assets, examining the notes as to their liquidity, and the securities as to their market value, in short, it seeks to establish that the resources and liabilities conform to their published value

A duplicate report is made in detail of the findings of the examination One copy is entered in the records of the clearing house, the other is sent to the president of the bank.

A more condensed statement is read before the clearing house committee. This report describes the character of the bank's assets in general terms. It points out all loans made either directly or indirectly to officers or directors of the bank or to corporations in which they are interested, and it describes all excessive and important loans. The examiner also gives his opinion of the soundness of the bank as he found it.

### **Audits of the Trust Department**

Certain classes of transactions made by the trust department are amenable to state laws, hence the department is examined by the state bank examiners as well as the national bank examiners in their regular audits. The law specifically limits the scope of state bank examinations to the work of the trust department. The inspection is conducted in the same way as national examinations and the findings of the audit are reported to the state banking department.

### **Audits by Bank Directors**

The board of directors of a bank are held responsible by the stockholders for the proper administration of its affairs. In line with this duty and also in conformity with the law which requires that they make an inspection of the bank at least twice a year, a committee from among the directors is appointed to perform this work. To assist them in these examinations the committee obtains the services of the general auditors of the bank, and the inspection follows along the lines of the general audit except that it is directed mainly towards verifying the assets of the bank.

## CHAPTER XXV

### THE FACILITATING OPERATIONS—MAIL, TELEGRAMS, CABLES, AND SUPPLIES

#### Nature of Activities

In the discussion up to this point certain operations which are wholly peculiar to a bank have been considered. It may be said that the functions mentioned in the foregoing chapters constitute the functions of the bank as such, they are the ones which distinguish a bank from a railroad company, a mining corporation, a department store, or any other type of concern. The complete work of the bank, however, necessarily includes many operations not peculiar to banking, that is, operations which are more or less common to all lines of business enterprise. In the words of A. W. Shaw,<sup>1</sup> these are the facilitating operations—the ones which facilitate the performance of the characteristic functions of the bank.

The facilitating operations may be divided into six classes.

1. Handling the mail
2. Handling telegrams and cables
3. Purchasing, printing, multigraphing, etc
4. Compiling and furnishing information to assist the management
5. Publicity
6. Personnel work and employees' welfare.

#### 1. Handling the Mail

The treatment of the incoming mail containing remittances has already been described in Chapter II on the work of the

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<sup>1</sup>See "An Approach to Business Problems," Chapter I

mail teller A large metropolitan bank with extensive banking connections, both domestic and foreign, receives a great volume of mail other than that containing cash items It is no less important that these letters be distributed promptly to those who are to give them attention than it is that cash letters be credited and the items collected without delay Accordingly an incoming mail department operating in two sections, domestic and foreign, and an incoming registered mail department have been organized to handle these letters

The outgoing mail in any large institution is best handled in a specialized department for the reason that expenditures for postage require some degree of supervision A bank has additional good reasons for centralizing the outgoing mail in specialized departments In the first place many shipments of valuables have to be sent out each day It is essential that a definite group of employees be held responsible for losses, inaccuracies, and delays In the second place a considerable part of the outgoing mail of the bank consists of letters for foreign countries The routing of foreign mail in such a way that it reaches the addressee in the shortest period of time is a business specialty in itself Hence to meet these needs an outgoing mail department consisting of two sections, the domestic and the foreign, and an outgoing registered mail department are in operation.

### **Incoming Registered Mail**

The incoming registered mail of the bank contains much of the currency shipped to the institution and many of the valuable papers received, such as notes, documentary drafts, stocks, bonds, etc The registered mail is obtained directly from the post-office With the various packages the post-office also delivers the receipt cards which are to be returned to the shippers of the packages, obtaining from the bank in lieu thereof a temporary receipt

Upon receipt the letters are numbered consecutively and entered in a received register in which they are described both by a departmental number assigned to them for reference and the post-office registration number. Special delivery letters and similar special items are entered in a separate section of the received register to assure immediate attention.

Each letter is opened and the contents examined to make sure that it contains what it purports to. In case a letter is to come to the attention of more than one department or person in the bank, transcripts are made for each of these persons or departments. The letters are then sent to the proper department by messenger. To insure accurate and reliable records of the deliveries the letters are entered in delivery books of which there is one for each delivery clerk. These books contain a complete record of the delivery, the date of the letter, the number assigned to it, the name of the sender, the post-office registration number, and the disposition, i.e., the department to which it is sent. As the letters are delivered someone who is authorized to receipt for registered mail signs the book in a space provided for the purpose.

### Notes and Coupons Received for Collection

Notes received for collection through the registered mail are handled in the same way as those received by the mail teller and the city collection department, viz., they are entered in an incoming collection blotter and delivered to the note teller, against receipt.

Mention has already been made of the fact that all coupons for collection, regardless of whether they come from outside the bank or not, pass through the incoming registered mail department where they are entered in a collection register which contains a control account for all coupons passing to the coupon collection department. If the sender has not already enclosed the coupons in separate envelopes according

to issues, the incoming registered mail department makes the separation and enclosure. When the collections pass to the coupon collection department these envelopes serve as the sole guide of that department, hence the following information is entered upon them: the name of the owner, his collection number, the collection letter date, description, number, and face value of the enclosed coupons, the total value of the envelopes, the due date, and instructions as to crediting the account or issuing a cashier's check to reimburse the customer.

### **Acknowledgment of Letter**

After examination of incoming registered letters has been made by the proper persons or departments the letters are sent to the mail teller for acknowledgment. Meanwhile in the registered mail department the receipt cards which the post-office customarily forwards to the senders of registered letters are prepared. At the close of the day these cards, which it will be recalled were obtained from the post-office with the mail, are checked against the delivery records and returned to the post-office to be mailed to the sender.

### **Domestic Non-Registered Mail**

In connection with the description of the work of the mail teller's department it was shown how all incoming non-registered domestic mail addressed to the bank comes first to this department which retains letters containing cash and collection items. The other letters are passed to a department known as the incoming mail department. To expedite the work this department operates in two shifts, the night and the day. If the address of a letter indicates for whom or for what department it is intended it is delivered to the addressee unopened. Other letters are opened, read, and stamped with the initials of the reader to fix responsibility for errors and are passed to the proper departments and in-

dividuals for attention. It frequently occurs that a letter must receive the attention of more than one department. In this case a sufficient number of photographic copies of the letter are made.

### **Foreign Mail**

Foreign incoming mail is handled somewhat differently from domestic mail. The domestic mail is divided into two portions, the cash mail and the non-cash mail. The cash mail is handled by the mail teller and the non-cash mail by the domestic section of the incoming mail department. Foreign cash mail, on the contrary, does not lend itself to the standard form of treatment used in the mail teller's department. Both cash and non-cash foreign mail is therefore received by the foreign section of the incoming mail department. Cash letters are sent to the foreign collection import department, while other letters are distributed just as is the domestic mail. Those letters which need to be translated into English before they are distributed are sent to the translator's department.

### **The Investigators**

In handling the large volume of business of a large bank, differences invariably arise between the bank and its clients. As explained in the preceding chapter the auditors investigate and rectify those differences relating to customers' balances. Differences and complaints which do not relate directly to customers' balances are investigated by a section of the incoming mail department known as the investigators.

When an investigation is undertaken a serial number is assigned to it for identification and a record is made in the complaint book. The complaint is then turned over to the department in which the error occurred and this department is responsible for a settlement with the customer. The complaint is followed up by the investigators who assure them-

selves that a satisfactory settlement is effected. Should the complaint be of such a nature that it cannot be properly handled by any one department it is attended to by the investigators themselves. In addition to allocating the error to the proper department, the investigators also ascertain who was responsible for it. A list of these errors is kept and forwarded periodically to the cashier of the bank.

### Work of Translators

As before noted many of the letters received from foreign customers of the bank must be translated before distribution to the operating departments. To meet this need the bank maintains a translator's department which translates not only letters but all reports, statements, and documents written in a foreign language.

It is important that clearing house items received from abroad be passed through the clearings on the day of receipt if possible, to avoid loss of interest to the remitter. To avoid delay in translation, translators are assigned during the early morning to the incoming mail department. On each foreign language remittance letter containing clearing house items, information sufficient to guide the foreign collection import department in making the collection is entered by the translators. After it is no longer possible to pass remittances through the clearings on the same day, there is, of course, no need for special haste and incoming remittance letters are translated in the regular way, except that they receive priority over non-cash letters.

In dividing the letters among the translators an assortment is made according to languages and those in each language are further classified according to their claims for prompt attention. The proper number of English copies are prepared, one copy of which is retained in the files and the others, after they have been checked for accuracy, are distributed to the



addressees. To fix responsibility for errors the translated copy is initialed by both the translator and the checker.

### **Translation of Outgoing Letters**

At the time a foreign account is opened the bank ascertains in what language the foreign customer desires to conduct his correspondence. A file showing what customers desire their letters to be written in a foreign language is kept by the translators. If a reply to an incoming letter is to be in the same foreign language a note to this effect is made on the letter. The recipient of the letter can thus ascertain without trouble whether his reply is to be made through the translator's department. Outgoing letters which must be sent in a foreign language are written in English by the writer, translated by the translators, and returned to the writer for inspection, signature, and mailing.

### **Outgoing Registered Mail**

A considerable portion of the outgoing mail of the bank consists of securities, money, and other valuables to be shipped by registered mail or by express through the outgoing registered mail department. When items are turned over to the department for shipment a record is made in a receiving book which gives a complete description of the transaction from what department it was received, to whom it is to be forwarded, the nature of the contents, etc. The package is then carefully wrapped and sealed in the presence of two members of the department who are responsible for the shipment until it is delivered to the carrier. Responsibility for an outgoing shipment containing the securities and other valuables is fixed by having the clerks in charge execute the following certificate

THE UNDERSIGNED, employees of the National City Bank of New York, hereby certify and affirm that the original of

the following letter, containing the securities specified therein, was this day sent by said the National City Bank of New York by registered mail, and they personally saw the contents of the package, and know them to be as stated in the letter, that said package was securely wrapped and sealed in their presence and never left their custody until deposited with and received for by the

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. . . . .

.....

. . . . .

New York

19 .

This statement is sent to the department from which the shipment was forwarded where it serves as a receipt

When the shipment is made the usual receipt is obtained from the post-office or from the express company After delivery the carrier returns a delivery receipt from the consignee Delivery receipts obtained in this way are checked against the receipts obtained from the shipping company at the time of acceptance of the shipment to make sure deliveries are made on time.

### Outgoing Mails

The procedure in handling the outgoing domestic mail of the bank presents no departure of particular importance The mail is assembled from the different departments of the bank by messengers and is weighed, stamped, and forwarded to the post-office All stamps used in the department are obtained from the petty cashier upon requisition and the cost is charged to the proper expense account of the bank

The work of despatching mail for foreign points presents certain peculiarities In the first place departures of mail steamers to some ports may be very infrequent In the second place many of the foreign letters contain shipping documents and it is essential in many cases that these documents reach

the addressee as soon as the corresponding shipments so that the consignee may avoid storage fees, customs, fines, etc. Hence it is important that the bank make sure the documents go forward on the same steamer as does the shipment or upon a steamer which is to arrive abroad at an earlier date. Finally, foreign items are commonly drawn in duplicate or triplicate and each copy is to be despatched by a different carrier. These conditions call for a specialized outgoing foreign mail section which maintains a record of sailing dates and is responsible for forwarding the foreign mail in the proper way.

### Sailing Schedules

The foreign section of the outgoing mail department has the function of keeping other departments in the bank informed of sailing dates for mail steamers. This information is obtained from a variety of sources such as commercial bulletins, post-office reports, steamship companies' reports, bulletins of exporting houses, and the daily papers. From the information thus gathered a weekly sailing schedule is prepared showing the names, steamships, their destination, dates of departure, whether each steamer carries United States or only consignee mail, and the closing hour for the mail for each steamer. A daily revision of the list is made on the strength of communications received from the various steamship companies. Copies of these schedules are sent to those departments of the bank interested in the foreign mails.

### Consignee Mail

While most steamships are regular carriers of United States mail, certain freighters carry only what is known as "consignee" mail. Consignee mail consists only of documents and letters pertaining to consignments of merchandise carried by the given ship. Such mail is delivered direct by the

sender to the master of the vessel, who mails it to the addressee when he reaches the port of destination. The purpose of consignee mail is to provide the shipper with a means of forwarding documents in such a manner that they will reach the consignee as soon as the shipment, regardless of the frequency of sailings of regular carriers. Consignee mail is carried only in rare instances to Europe or the Orient but is general in the South American trade. Certain countries impose heavy fines upon the importer if it becomes necessary to store goods after their arrival at the foreign port because documents have failed to arrive.

### Forwarding Foreign Mail

Except for single-copy letters, the work of forwarding the foreign mail begins with the operation of enclosing the material in the envelopes. As items are received from the various departments they are sorted according to countries of destination, the originals and duplicates are separated, and each package or letter is wrapped and routed according to the steamer on which it is to be sent. Originals are routed via the vessel which is likely to reach the destination first and duplicates go forward on the next one. The mail is then turned over to the post-office department or to the steamship company in time to be placed aboard ship.

Mail which has not been prepared in time to reach the post-office at the regular advertised closing hour for that particular shipment may be sent later, provided twice the postage usually required is paid. The extra postage is for the purpose of reimbursing the post-office department for the labor involved in rushing the mail to the steamer. Such mail is called "supplementary" mail.

The bank's interest in the mail does not cease with the delivery of the letters and packages to the post-office or steamer. In connection with the work of the traders, mention

has already been made of the importance of knowing when letters containing remittances arrive abroad and become available for the use of the bank. To meet this need careful watch is kept over arrivals of ships at the foreign ports in order that the necessary information may be sent to the traders.

## **2. Telegrams and Cables**

The work of handling telegrams and cable messages is performed by the telegraph and cable and the test words departments. The former has the duty of receiving and transmitting messages and accounting for their cost, the latter affixes test words to outgoing messages and verifies those appearing upon incoming ones.

### **Codes**

To reduce the expense of sending telegrams and cables and to obtain a degree of privacy, messages are frequently sent in code. Many financial institutions and other large concerns have their own code system which they and their customers use in sending messages from one to the other. Other concerns use one of the commercial codes of which there are a considerable number on the market. For the convenience of itself and its customers the bank has its own private code. In addition to the code of the bank the telegraph and cable department is equipped with key books for reading commercial codes and the private codes of whichever of the bank's customers and correspondents have issued them. A list of those who are in possession of the bank's own code is also kept in order that it may be used in as many cases as is possible.

### **Incoming Messages**

Incoming telegrams are transcribed in triplicate. If a particular message comes in code, the code version is placed

at the side of the English version in order that all information may be readily available should a question arise concerning the accuracy of the translation from the code. A time stamp is placed on the original copy, then it is forwarded immediately to the person or department who is to give it attention. The duplicate of the transcription is filed, while the third copy is held by the telegraph operator.

Cable messages, especially, frequently contain information which is intended for more than one department or individual. To distribute these messages, as many copies as there are subjects contained in the message are prepared. For convenience these subjects are divided into five classes as follows:

- 1 Cash payments
- 2 Transactions under commercial credits and delivery of documents.
- 3 Customers' securities.
- 4 Bond orders.
- 5 Miscellaneous

No	SIGN AND RETURN TO TELEGRAPH & CABLE DEPT	97989
97989	Nº 97989	
	FULL NAME <i>John R. Brown</i>	
	DEPARTMENT <i>Note Teller's</i>	

Form 97 Telegram Receipt (Size 8 x 2)

In preparing copies of the message, paper of distinctive color is used for each subject. Matter irrelevant to the subject to which the particular copy pertains is stricken out and the copy is forwarded to the proper individual or department for attention.

In order that the progress of the message through to its destination within the bank may be traced and responsibility

fixed for delays and loss of items, a serially numbered receipt system is used in making all deliveries. The receipts (Form 97) of which there are distinctive colors, one for telegrams and another for cables, are divided into three sections, each of which bears the same serial number. When a message is ready to be delivered to some department or individual in the bank, the first and second sections of the receipt form are attached to the message and the third section is retained for the files. On this third section is written such information as will indicate the disposition of the message. The individual who receives the message signs his name and indicates his department on the second section of the receipt form, which he then returns to the telegraph and cable department. The first section remains on the message as a reference number. Each day the slips on file indicating the numbers sent out are compared with the receipts returned, to make sure that all messages have been delivered.

### Confirmations

It is an almost universal practice to confirm telegrams and cables by sending the recipient a letter informing him that a message has been sent and giving a transcript of it. Incoming confirmations are received by the incoming mail department and are routed to the department which received the original message. It is also customary for the recipient of a message to mail an acknowledgment to the sender. For this purpose a carbon copy of the message is sent out by the telegraph and cable department.

### Outgoing Messages

Outgoing telegrams are prepared (in code, if necessary) by the department in which they originate. Each telegram is made up in three copies. The original is retained by the telegraph and cable department as a record of the message.

The duplicate, which serves as a confirmation of the message, is forwarded to the addressee, while the third copy is signed for, stamped with the time of transmission, and returned to the sending department as evidence that the message was despatched on time. In sending outgoing cables six copies are used. In addition to the copies serving the purposes mentioned in connection with telegrams, there is a copy of the message for the officer who is in charge of the territory of the recipient, one for the foreign files, and one for the bookkeepers of the telegraph and cable department.

Telegrams are sent to the telegraph companies by means of instruments operated in the department. Cable messages are transcribed in code and transmitted to cable companies by messenger. In addition to the copy of the cable message which is delivered to the cable company, one copy is retained by the bank for reference and a second copy is signed by the company and returned to the bank where it serves as a receipt.

### Private Wires

Many financial institutions have their own private wires connecting their head offices with those of out-of-town branches and correspondents. This arrangement has the advantage of absolute secrecy and it secures undivided attention to the despatching of the institution's own messages. Through an arrangement with a closely affiliated concern, the bank upon the practices of which this is written has the use of private wires running to practically all the chief cities of the United States and Canada.

### Accounting Procedure for Messages

If the cost of telegrams and cables is to be borne by the customer, one of the accounts termed "Customers' Expense Fund account—Telegrams," "Customers' Expense Fund account—Cables Incoming," or "Customers' Expense Fund



account—Cables Outgoing,” is credited. These accounts represent the liability of the bank to pay the various telegraph and cable companies funds which it has received from customers in cover of messages. The customer settles with the bank either by sending a remittance or by having his account charged, and the resultant debit to cash or to the customers’ deposit account serves to offset the credit to Customers’ Expense Fund.

In many instances the customer does not furnish reimbursement at the time the bank incurs the obligation to pay for the message. In such a case the bank charges the cost to that particular customer’s account under one of the control accounts termed “Accounts Receivable account—Telegrams” or “Accounts Receivable account—Cables.” This charge offsets the usual credit to Customers’ Expense Fund account—Telegrams, or Customers’ Expense Fund account—Cables. When the customer sends a remittance the department receiving it credits his account in the Accounts Receivable account—Telegrams, or the Accounts Receivable account—Cables ledger.

Monthly, or at other stipulated intervals, the bank settles with the various cable and telegraph companies for the cost of messages received collect and of those not sent collect. Incoming bills are paid through the voucher register. That part of the costs which relates to the bank’s own messages is charged to the Expense account, while that which was incurred for customers is charged to Customers’ Expense Fund account—Telegrams, or Customers’ Expense Fund account—Cables.

### Use of Test Words

As indicated in preceding chapters, a test word serves the same purpose in relation to a cable or a telegram as a signature does to a written instrument. In order that the recipient of a message may be sure it comes from the one who purports

to be the sender, the latter attaches some word which is built up in a manner known only to the two parties concerned

It is apparent that the work of preparing and transmitting the bank's own test word system to customers who have occasion to use it, of filing information which will enable the bank to decode the test words of other institutions, and, finally, of verifying incoming messages by means of the test word, is necessarily confidential and secret. These tasks are performed by the test words department. When a message ordering cash payment is received it is forwarded to the test words department where the test word is proved before the telegram is delivered to the proper department. Outgoing messages likewise pass through the test words department where the bank's own test word is appended.

### 3 Supplies

The economical purchase and control of the supplies used by the bank is effected through four departments. These are.

1. The purchasing department
2. The stationery department
3. The printing department
4. The multigraphing and typewriting department

The purchasing department is organized in sections, each of which attends to purchasing materials and supplies of only one class or kind. Thus there is a printing section, a stationery section, an office furniture section, etc. This method of organization makes it possible for members of the department to familiarize themselves thoroughly with the types of merchandise and market conditions in their special lines and to obtain the best prices, prompt deliveries, etc.

### Requisitions and Orders

An order for supplies to be purchased originates in the department which is in need of the supplies. The order

originates from a requisition signed by the department head and division head. The requisition receives the approval of the organization department, which exercises final control over expenses of the bank, after this it is passed to the purchasing department, which obtains bids for the supplies requested and then places its orders with the bidder submitting the best price

At the time the order is placed the date on which the goods are to be delivered is specified. One copy of the order is filed in a tickler under the delivery date so as to bring it to attention in case it is not executed promptly. Four other copies of the order are made. The original is for the dealer, the second copy for the accounting department—which, as has been noted, prepares the voucher and makes the payment—the third for the stationery department, and the fourth copy for the receiving room.

When orders are delivered to the receiving-room a notice of delivery is prepared in triplicate. One copy of this notice is sent to the voucher register where it serves as authority to make payment, a second copy is sent to the purchasing department, and a third is filed in the receiving-room. When a notice of delivery has been received the goods are inspected by the purchasing department and if they are found to be as ordered the transaction is approved. The order, together with the report of the receipt of the goods, is then filed away in a filled order file the purpose of which is to furnish a record of purchase in case other supplies of a like nature are needed in the future.

### Printing

The printing work of the bank is also cared for by the purchasing department, which receives bids and enters into contracts for outside printing for the bank in the same manner in which it makes its orders for supplies. The bank, however,

maintains a small printing department chiefly for the purpose of printing customers' checks.

The manner in which the checks are prepared and the form which they take is governed entirely by the instructions of the customer. A record showing the numbers of the first and last checks issued to each customer is kept in order that the bank may know what numbers to assign to additional checks ordered.

### **Addressograph, Multigraph, and Typewriting Department**

The bank necessarily has extensive mailing lists for various purposes. First there are monthly statements of account and form notices to be mailed to customers. Second there are extensive lists of names to which the publicity department sends its publications. Then there are lists of stockholders used by the transfer department in mailing notices, dividend checks, etc. Finally there is the list of employees from which the salary envelopes are prepared. The work of keeping these lists up to date and addressing material to be sent out is done by the addressograph, multigraph, and typewriting department. In addition to the mailing lists, this department prepares the form letters which the bank sends out.

### **The Stockroom**

The stationery department of the bank performs the function of a stockroom. Delivery of supplies is made only upon a requisition signed by a department head and a division head. The filled requisition forms are turned over to the purchasing department where they are filed according to departments receiving the supplies. At the end of each month statistics are prepared showing the amount of supplies used by each department. This report is submitted to the auditors where it is used for the purpose of maintaining a control over supplies.

Another function of the stationery department is to see that an adequate supply of the materials used in the bank is kept on hand. A supplies book, which contains a perpetual inventory of the supplies on hand, serves as a reminder when quantities are running low. When a given minimum amount of any class is reached, requisition is made upon the purchasing department for whatever is needed.

## CHAPTER XXVI

### THE FACILITATING OPERATIONS—LEGAL AND STATISTICAL INFORMATION, PUBLICITY, AND PERSONNEL WORK

#### 4 The Internal Information Service—Legal Department

As an advisory bureau regarding legal matters the bank maintains a department known as the internal legal department

The internal legal service is concerned with the legal phases of all claims and disputes which have not yet reached the litigation stage. These include cases of forgery or check alteration, examinations of the legal aspects of collateral, especially the legality of the issuance of bonds offered for collateral, the legal phases of payments on checks and bond coupons, requests for reimbursement on account of checks paid over stop-payments, requests for reimbursement because of lost checks, and other similar cases. In case the bank issues duplicates to reimburse customers for lost cashier's checks, certified checks, etc., the necessary guarantees, affidavits, or indemnity bonds are obtained by the legal department. Injunctions and legal notices received by the bank, together with notices of the death of depositors, are also cared for by this department.

Two other phases of the internal legal service are worthy of note. First there is the insurance work. In this connection a periodical analysis of the bank's insurance is made and all claims arising under existing policies are prepared and followed up. All charges for premiums come to this section and are checked before payment is made. Second there is the work of caring for the items of the Suspense account. The Suspense

account has already been described—it contains the doubtful accounts of the bank. Complete charge of these items is taken by the legal department and they are followed up and collected if possible.

### Financial Library

The financial library of the bank has two functions, that of keeping books, periodicals, etc., for reference, and that of collecting and filing information regarding the financial affairs of corporations and municipalities.

The primary object of the first-mentioned function is to make available within the bank all information needed for making whatever studies and investigations are required in the daily work. Accordingly a complete set of public documents of all countries, reports of chambers of commerce and similar bodies, laws and statutes of the United States, yearbooks, almanacs, directories, maps, and financial periodicals, is kept. A secondary object is to keep on hand for general reading by employees books pertaining to business in general, hence books on banking, finance, exchange, etc., are distributed to those connected with the bank under the same conditions as in public libraries.

The second function of the bank library is to gather credit information concerning municipalities and corporations which have securities outstanding. Accordingly a section of the library devotes its attention to preparing clippings from financial publications and to gathering such information as descriptions of mortgages securing bond issues, bond and stock offerings, deposit agreements, documents concerning municipal and government finance, etc.

### Statistical Work

The internal statistical service of the bank consists in making researches regarding commerce, production, industries,

transportation, financing, economics, etc., in order to provide the administration with such information as may be of service in formulating the broader policies of the bank. The work is also closely related to the publicity work of the bank, various studies of the department are distributed in pamphlet form and certain of the information contained in other publications of the bank is supplied by the statistical department.

## 5 Publicity

Bank publicity is mainly of the direct type. General display advertising in newspapers and magazines is used incidentally, as when, for example, a bank publishes its financial statement in accordance with the call of the Comptroller of the Currency. Occasionally a general medium will be used to emphasize and introduce some new service of the bank, but as a rule the bank's publicity work consists in mailing its advertising material directly to a selected mailing list.

The advertising material issued is educational in nature. An idea of the nature of a bank's efforts in this direction can probably be best conveyed by giving a brief description of the material sent out by the bank upon the practices of which this book is written.

This bank, for example, issues a monthly bulletin on "Economic Conditions, Government Finance, United States Securities," which contains discussions of current economic and business conditions and an analysis of the social and governmental problems of the day. The bulletin is prepared by a vice-president of the bank, who is a practical economist. Its aim is to promote the good-will of the institution, hence it is widely circulated not only among clients and prospective new customers but also among leading business and professional men. In addition to the English edition which circulates in the United States, Great Britain, Canada and other British colonies, French and Spanish editions are published for circu-



lation in countries using these languages. Certain of the branches of the bank issue similar publications dealing with conditions in their respective countries.

As a constructive service for correspondents, such a bulletin may be furnished at the cost of printing to those who desire to distribute it in quantities to their customers. When the bulletin is furnished in this way, it would appear as the publication of the bank by which it is prepared, but it also contains whatever advertisement the correspondent desires to have inserted.

### **Special Bulletins, Addresses, Exhibits, etc.**

In addition to the monthly bulletin, special publications contribute to the bank's fund of material for developing general good-will. These are prepared by various officers and other experts in the employ of the bank. They contain informative material which the bank wishes to place in the hands of its clients but which needs treatment in more detail than the limited space of the periodical publications will permit. The circulation of these booklets depends upon their contents. Some, for instance, might be of interest only to a particular class of business man or to those residing in a particular territory and the circulation would be limited accordingly. Others, say those dealing with some phase of the economic position of the country, are of more general interest and they are accordingly widely distributed.

Supplementing these efforts there are the addresses of officers of the bank delivered before meetings of various associations of business men. It is the policy of the bank to contribute to the discussion in gatherings of this sort whenever it is called upon to do so, provided, of course, someone of the bank's staff who can be of real service is available. Frequently also the bank arranges exhibits at fairs and other meetings of this sort.

### Publications for Promoting Foreign Trade

The awakened interest in foreign trade among American business men has led to a considerable portion of the publicity work being devoted to disseminating authoritative information on this subject. A monthly magazine, known as the *Americas*, contains articles on the various phases of foreign trade, trade reports from the bank's representatives abroad, articles giving commercial and historical surveys of foreign countries, surveys of international industries, etc. A report issued weekly by the statistical department analyzes trade statistics for clients of the bank and presents such facts regarding exports, imports, and the production and consumption of specific articles which enter into international commerce, as will be of assistance to traders. Finally should be mentioned a report issued weekly by the foreign trade department for the purpose of bringing specific opportunities for trading to the attention of American business men.

While various officers and other experts in the employ of the bank are called upon to contribute to the material for the bank's publicity efforts, the work of preparing and keeping the mailing lists up to date, of editing the material, and of publishing the periodicals and booklets is centralized under the control of the publicity department. In addition to attending to the physical production of the material, this department, acting under directions of a vice-president who is in charge of publicity, determines the direction which the bank's publicity efforts shall take.

### 6. Personnel and Related Activities

The scope of the personnel work of the bank may be indicated by the following outline of the activities of the personnel and related departments

- 1 Engaging new employees
- 2 Transferring employees

- 3 Attending to resignations and discharges
- 4 Answering inquiries from those who have been referred to the bank by former employees
- 5 Making job analyses
- 6 Making studies of the salary question and preparing statistics regarding the working force
- 7 Interviewing employees and keeping data regarding the relations between employees and the institution
- 8 Maintaining an employees' club.
9. Conducting educational work among employees.
- 10 Doing welfare work among employees

These functions are distributed among four departments—the personnel department, the educational department, the employees' club, and the medical department. The personnel department has charge of the work of employing, transferring, and discharging help, and of performing the necessary auxiliary functions. The educational department has for its function the promotion of educational endeavor among employees. The medical department, as its name implies makes examinations of all new employees and its services are at the disposal of all members of the bank's staff who are in need of medical attention while engaged in their daily duties. The club is an organization of the employees of the bank which has for its aim the promotion of the welfare of its members.

### Employment of New Help

Applicants for positions with the bank, whether they come to the bank on their own initiative, from an employment agency, through the introduction of an officer or a friend of the institution, or in reply to an advertisement for help wanted, come into contact with the personnel department where they are required to file a standard form of application blank. Along with other data the applicant submits the names of references which are to be consulted by the bank. The

personnel department obtains opinions of the applicant from these references and files them with the application form. The information contained in this file constitutes the basis for deciding the question of employing the applicant should need for his type arise.

Vacancies in the force of the bank come to the attention of the personnel department in the form of requisitions signed by the department head and the division head in whose provinces the vacancy occurs. By means of a system whereby requirements for particular positions have been analyzed and uniform standards set up, the division head is enabled to communicate a full description of the qualifications which the prospective employee must possess by merely indicating on his requisition the job number of the vacancy. After the requisition has been received, the most promising one from among those who have applications on file is employed.

Each employee of the bank is required to furnish bond, the purpose of which is to protect the bank against losses for which he might be responsible. These bonds are obviously a form of insurance. The cost is therefore borne by the employer just as is the cost of other insurance. Through the personnel department the new employee submits application for a bond to the surety company with which the bank deals, and this department is also charged with the duty of making certain that the new employee has been approved by the insurer before he enters upon his new duties.

Frequently the necessity for transferring an employee from one department of the bank to another presents itself. Aside from shifts in the volume of the work which creates an over-supply of workers in one department and a shortage in another, these transfers often become necessary to serve the interests of harmony. Transfers are made by the personnel department which acts in conjunction with the division heads and the department heads concerned.

In a large institution the needs for temporary stenographic service in the various departments are so numerous as to require the maintenance of an emergency force of stenographers and typists. Employees just entering the service of the bank are generally assigned to this force, since the work is such as to give them wide acquaintance with the bank's work as a whole.

### Resignations and Discharges

When it becomes necessary for the bank to discharge an employee the case is handled by the personnel department, also formal resignations from all who are leaving the employ of the bank are obtained. From the data obtained in this way statistics are prepared covering the causes which prompt employees to resign. These statistics prove useful in indicating points of disturbance in the personnel problem and in assisting the department in making recommendations to the administration for remedying the condition.

Naturally former employees who have left a good record behind them give the name of the bank as a reference when applying for positions elsewhere. Inquiries arising from references are answered by the personnel department.

### Interviewing Employees

An important phase of the work performed by the personnel department consists in interviewing employees. Through these interviews a personnel relation is maintained between the institution and its employees. A sincere effort is made to locate any cause of dissatisfaction and to apply the remedy.

To enable the man to be better fitted to the job, a detailed analysis of each position in the bank has been made. From these analyses records showing the qualifications which the incumbent must possess have been prepared. To each job is

assigned a number by the use of which the division head designates his needs for new employees. The job analysis work therefore amounts to setting up certain standards for describing workmen and their tasks, just as in other lines of endeavor there have been set up standards for measuring commodities, distances, etc.

### Salary Standardization

Periodical analysis of the salary schedules of the bank together with recommendations for increases are prepared and submitted to the management for action. Consideration and approval of recommendations for promotions and salary increases are also made by the personnel department. Through these activities, equal rates of remuneration for tasks of the same type are enforced and the stigma of favoritism in promotions and salary increase is avoided.

### Records, Reports, and Statistics

To facilitate the personnel work several records are kept. Most important are the employees' folders. In each of these folders is kept complete information regarding an employee, his original application for a position, the reports obtained from his reference, reports of those immediately in charge of his department, results of interviews of the personnel department, etc. A list of the employees arranged alphabetically and by departments is also kept so that an employee may be readily located in case of inquiry or other need. The bank also has specimen signatures of each person in its service.

Absence of employees from work is checked up by means of the time-clocks. Each day a report is sent to the cashier, to the comptroller, and to the organization department, showing the total number of employees in the bank and the absentees. After an employee has been absent for five consecutive days the cause of the absence is investigated by the personnel

department and if the employee is in distress the assistance of the bank is brought to bear upon his problem.

Detailed records of the number of applications received, the number of new employees hired, the sources from which they come to the attention of the department (employment agencies, classified advertisements, or introduced), the departments to which they are assigned, their religion, sex, nationality, etc., are also kept, as well as reports conveying similar information regarding resignations and the reasons therefor. Periodically these reports are put in condensed form and submitted to the comptroller of the bank.

The summary of this report shows the labor turnover of the institution for the current period and for the corresponding periods of previous years. Two turnover figures are submitted—the gross and the net. The gross figure is obtained by dividing the total number of resignations for the period by the average daily attendance. Mainly this figure is useful for comparing general conditions during the period under consideration with those obtaining in previous periods. The net turnover rate is obtained by dividing the resignations for avoidable reasons only by the average daily attendance. Such a rate is in a measure an index to the efficiency of the personnel work of the bank, since it shows a percentage figure of employees who under ideal conditions might have been retained.

### **The Employees' Club**

The activities of the employees' club of the bank constitute virtually a part of the personnel work. The club is organized as an institution separate from the bank, being operated solely by the employees of the institution. It has been permanently endowed by the bank from which it also receives direct financial aid at times.

Among the chief activities of the club, all of which aim at promoting the welfare of the employees, may be mentioned

- 1 Publishing a monthly magazine for employees
- 2 Provision for outings, theater parties, and other forms of recreation for members.
- 3 Maintenance of athletic teams
- 4 Maintenance of a saving bank, a co-operative store and buying service, and other devices for promoting thrift among employees
5. Operation of a realty corporation for assisting members to purchase or build their own homes on advantageous terms
6. Providing educational courses for members.

### **Mutual Benefit**

The mutual benefit work of the bank takes a variety of forms Temporary financial assistance is extended to those who find themselves in need, medical attention and liberal leaves of absence are provided for those in poor health, etc In addition there are some few welfare activities which take a more or less regular form All new employees are examined by the medical department as a condition precedent to employment and those who may find it necessary to consult a physician while attending to their regular duties are served without charge A pension system is provided for the retirement of employees who reach the age of sixty and for the payment of a liberal portion of their salaries by the bank during the remainder of their lives Under a death benefit plan benefits are paid to heirs of an employee should death occur while in the bank's service

### **Educational Activities**

The educational activities of the bank may be divided into two parts (1) training new employees, and (2) promoting the educational advancement of employees

*Training New Employees* Those who come into the



bank's employ as messengers, pages, and other of the beginners' grades are required to attend regular instruction in preparation for their work. In addition a large part of the personnel for its foreign branches is recruited and trained by the bank through its college training class. Under this arrangement the bank selects employees some time before they complete their college courses. Each prospective employee attends college as a regular student and the faculty of his educational institution sends the personnel director of the bank detailed reports covering his progress while at college. During his summer vacations the student takes up his residence in New York where he attends special educational classes given by the bank. The aim of these courses is to supplement college training with technical knowledge of banking, languages, foreign trade, etc. In addition to his regular classes, the student is assigned to various departments of the bank in logical succession where he serves in the capacity of a regular employee. Thus he obtains a first-hand knowledge of banking by the laboratory method. After graduation the student enters the bank's employ in some one of its foreign branches.

*Co-operation with Local Educational Institutions* In its educational activities the bank co-operates with established educational institutions in so far as is possible. It brings courses being offered by the various institutions of the city to the attention of employees, and upon their enrolling in classes approved by the educational department it pays a portion of the tuition fee. Located as it is in a city where educational facilities abound, the bank is enabled to obtain for its employees the best of instruction in a wide variety of subjects without the necessity of maintaining a large force of instructors. For subjects pertaining to the immediate field of banking and for the benefit of employees who are of the age required by the laws of the state of New York to attend instruction, however, the bank conducts its own classes

## CHAPTER XXVII

### FOREIGN TRADE, MERCHANDISE, AND INDUSTRIAL SERVICE

#### Service

The prosperity of a bank is wholly dependent upon the volume of business handled by its customers. Realizing the importance of this fact, a successful bank is constantly on the alert to further the interests and assist in extending the business of its customers in every legitimate way. The bank's efforts in this direction are not confined to the activities of any one department or any group of departments. Each of the departments, rather, performs whatever constructive services its activities warrant, as has already been indicated in preceding chapters. In addition the whole scheme of administration in the bank is patterned to furnish intimate personal service to clients, as will presently be shown. In the bank specially under attention there are, however, three departments designed primarily to promote the interests of the bank's clients and of trade in general—the foreign trade, the merchandise, and the industrial service departments. The foreign trade department aims chiefly to expand foreign trade, the foreign merchandise department assists in the actual exportation, importation, and transshipment of merchandise, and the industrial service department advises customers on industrial problems. These are primarily service departments, but they contribute to the income of the bank inasmuch as they act as feeders for other departments.

#### FOREIGN TRADE SERVICE

The daily operations of a large international bank bring it into close touch with all phases of business. Especially in

the United States where many business men are just beginning to enter the field of foreign trade on an extensive scale and are naturally perplexed with such problems as obtaining credit information, selecting foreign agents and representatives, choosing proper channels of distribution for their products, packing, shipping, financing, etc., a bank of this sort is enabled to furnish a high type of service in furnishing foreign trade information to its customers, both domestic and foreign. In so doing it assists in establishing actual business connections between foreign and domestic traders from which it has the benefit of the resulting banking business.

### **Organization of Department**

In order that the service rendered by the foreign trade department may be of the greatest practical value the personnel must consist of men who have had wide experience in foreign trade. The staff is divided into two sections—a domestic and a foreign. On the domestic side the division of labor conforms to the official territories of the bank, i.e., by states. A thorough study is made of the products which each section of the country contributes toward the export trade and of those foreign goods for which there is an actual or a prospective demand.

The foreign section is necessarily composed of men who have had extensive commercial experience abroad and who therefore are thoroughly acquainted with the customs, psychology, and commercial life of foreign peoples. These men are likewise assigned to the districts with which they are most familiar. By this arrangement the department is able to give intelligent consideration to concrete problems.

### **The Branch Bank as Promotion Agency**

One of the primary objects attained in a branch bank organization is real, live attention to the needs of American

interests in the foreign field. It is felt by many that in dealing with most countries the branch bank system has an advantage over the correspondent bank method of transacting international banking business, in that the branch bank has the American viewpoint of the foreign field and is therefore primarily a servant of the American business man. The basis of the work of the foreign trade department is therefore to be found in complete and accurate investigations conducted by such foreign branches as the bank may have. The branches have special representatives who devote their entire time to studying trade conditions and searching for new prospects and business opportunities in their particular districts.

The results of the investigations of the branches are embodied in reports rendered to the home office. These reports are of four kinds:

1. Commercial reports
2. Industrial reports
3. Trade reports
4. Miscellaneous reports

Commercial reports deal with trading concerns, industrial reports with manufacturing establishments, trade reports cover the field by commodities, and miscellaneous reports treat a variety of subjects, such as government legislation, trade-mark laws, customs and tariffs, general shipping news and facilities, public works, firms or individuals suitable to act as agent for United States concerns, etc. Under this arrangement the foreign branch of the bank is put at the disposal of each domestic customer.

In addition to the regular reports, information on specific trade opportunities is frequently forwarded on request. Whenever the bank has no branch a correspondent of the institution looks after foreign trade promotion in a similar way. A trade report would include information on the matters listed and outlined below:

## SUGGESTED OUTLINE FOR TRADE REPORTS

- 1 General demand for article  
Comparison of quantities imported in prosperous and bad years  
Imports for the last year obtainable  
Native production for last year
- 2 Past and present sources of supply  
If there has been any change in the source of supply, reason of such change  
Description of native industry
- 3 Present demand and stocks on hand
- 4 Prices, freight, duties, etc  
Invoice price from competing markets  
Invoice price from U S A  
Freight on article from competing markets  
Freight on article from U S A  
Landing charges  
Duties (incoming) from competing markets  
Duties (incoming) from U S A  
Cost of placing article in your market from competing countries  
Cost of placing article in your market from U S A  
Cost of native article  
Prices obtained from ultimate consumer
- 5 Terms of payments
- 6 Reasons, if any, why foreign or native article has been preferred to American  
General description of article as imported or manufactured in your market
- 7 Foreign competition—giving details
8. Manner of packing  
Labels, etc
- 9 Suggestions for improvement in article, manner of packing or labels, etc, which might appeal to the trade
- 10 Description of how business in article is done, and through what hands it passes from the manufacturer to ultimate consumer  
Class of people who ultimately purchase the article
- 11 Uses peculiar to your market, to which the article is or may be put
- 12 Advertisement if any.
- 13 General summary

### Distributing the Information

The main function of the foreign trade department, in the bank already referred to, is to collect these reports, coming from all parts of the world, condense and combine them, and distribute the information to clients of the bank. Distribution is effected in three ways

1. By the publication of a weekly bulletin entitled *Foreign Trade Opportunities*
2. By direct replies to letters of inquiry.
3. By interviews

*Foreign Trade Opportunities* Opportunities for American business houses in the foreign markets, after careful investigation, are published in the weekly *Foreign Trade Opportunities* and mailed to those domestic clients who have expressed a desire to receive this circular. Only a general outline of each opportunity is given in the announcement, but to those who are sufficiently interested to apply for it, complete details are furnished in the form of a special report.

The topics covered in this bulletin are: (1) names of foreign visitors in New York who desire to make immediate business connections, (2) foreign concerns which have written to the bank of their desires to buy or sell, (3) names of those desiring to represent American concerns abroad or seeking representation in the United States. In addition foreign trade reports are issued, dealing with specific products and information on topics of general interest to importers and exporters.

The usual non-liability clause similar to that used in distributing credit information is appended to the *Foreign Trade Opportunities* as follows

All statements or opinions herein contained are based upon the information derived from sources considered reliable, but are submitted gratuitously, and no responsibility is assumed by or is to attach to this Bank or any of its officers

While it assumes no responsibility the bank naturally exercises the utmost care in bringing together only reliable concerns in both countries. In fact, the strong point in the foreign trade service of such a bank is the extreme care taken in compiling the information given out.

*Letters of Inquiry* Letters of inquiry applying for information of other sorts frequently come to the bank. They cover a variety of subjects, in fact, any subject related to foreign trade may be included. These letters are made the subjects of special investigations. Within the bank such sources of information as the financial library, and the statistical, the foreign merchandise, the publicity, and the credit departments are utilized, according as the needs of the case bring the investigation beyond the files and knowledge possessed by the foreign trade department. Outside the bank, experts along certain lines, the United States Bureau of Foreign and Domestic Commerce, and similar agencies may be consulted. The bank may also request its branches, traveling representatives, and correspondents to obtain information from their particular territories. In short, the customer of a bank of this type is assured of the broadest possible investigation of problems he may lay before the foreign trade department.

Whenever reports are received in response to special inquiries from clients, a digest is made and forwarded to the client. Sufficient time is then given for these parties to make full use of the information, and after that it is as a rule published in the usual way for the general information of the bank's clients.

*Interviews* Local clients of the bank frequently call in person to discuss their problems. These interviews cover a great variety of subjects ranging from the definition of technical terms to the organization of an export department, or from methods of packing merchandise to systems of gov-

ernment in remote regions, but they usually have to do with concrete immediate problems which confront the client.

### Prospective Visitors to Foreign Countries

Valuable assistance can be rendered by such a department in many ways to the client who is preparing to go abroad. The members of the foreign section are in a position to give him the benefit of their experience acquired through residence abroad. The client may confer with the heads of the various foreign departments of the bank in regard to his plans. Letters of introduction to the branches, correspondents, and other customers of the bank are also written in his behalf so that when he arrives abroad he will have the local facilities of the branches and correspondents of the bank at his disposal. In this way every possible assistance can be given the customer in his undertaking.

### Foreign Visitors

The facilities of such a department in a large international bank are designed to be of equal benefit to the foreign client who is visiting this country. The foreign business man in the course of his visit to the bank may be referred to the foreign trade department by the officer in charge of the foreign district concerned. The foreign trade man of that district, speaking a language known to the visitor and appreciating his methods and point of view, is in a position to serve his needs in the most effective manner. If the client has a product to market in the United States every effort is made to bring it to the attention of the bank's clientele in the country. As has already been indicated this may be done through such a bulletin as the *Foreign Trade Opportunities*. A conference may also be called with the member of the department in charge of the domestic district in which there is most likely to be a demand for the particular commodity, or if the product is one for



which the market is wide-spread all the members of the domestic section may be consulted. Reports may also be prepared on the different concerns with whom the representative may care to deal.

The visitor from abroad is urged to make the department his headquarters while in New York and there meet representatives of American concerns. If he desires to travel about the country, letters of introduction to correspondents and customers of the bank are given him. In a word, the home office of such a bank and its extensive system of domestic correspondents are put at the disposal of business men from abroad, to each according to his particular needs.

### Miscellaneous Services

The miscellaneous services of the foreign trade department of an international bank may be illustrated further by the commercial directory in Spanish and Portuguese issued by one such bank for distribution by its branches. In preparing this directory the idea was to put into the hands of foreign business men an up-to-date publication by means of which they could locate the names of prospective customers or sources of supply for establishing closer connections with the United States. This directory is composed of two sections: a list of all the business houses which the bank numbers among its domestic customers, and a list of the commodities with the names of the firms which deal in them. Under the name of each concern is shown the cable address, the codes, it uses, when established, the capital and surplus, the names of its agents abroad, if any, the product manufactured or dealt in, and a statement as to whether it does an export and import business or not.

Note is taken of all important conventions and similar public functions which may be used to the advantage of the bank in developing its relations along the lines of foreign

trade, for the purpose of assisting the publicity department to make the proper contribution to the discussion

The first to benefit from such a foreign trade service, of course, are the clients of the bank. It is for them that the department is established in the first place. However, as the bank takes a broad view of its duty and responsibility it generally assists in so far as prior claims permit, all worth-while organizations and individuals. In facilitating these trade connections the bank, while assuming no responsibility for results, takes every precaution to bring together only parties of approved standing in order to safeguard its own name, to protect the interests of its clients, and to build up good-will for American business in general.

### **Foreign Merchandise Service**

In the course of its regular operations it does not often happen that the bank has to concern itself with the actual handling of goods. Occasionally, however, it may prove desirable for a customer located abroad or at a considerable distance from New York to appoint the bank his agent, giving it a lien or title to shipments of merchandise. The bank at times also takes over insurance claims, makes payments on ships under construction, and undertakes collections of an irregular character for the account of its clients. These services are performed in the bank under attention by the foreign merchandise department. This department occupies in the foreign division a position somewhat similar to that of the note teller and the city collection department in the domestic division.

### **MERCHANDISING SERVICE**

Custom house procedure requires that import shipments be claimed immediately upon their arrival in port, otherwise the goods are seized and stored by the government with a resultant heavy charge to the shipper. To avoid this con-

tingency the bank, as the only representative of the shipper on the spot, temporarily takes charge of its customers' shipments which are being held up and cares for them pending ultimate disposition. Such action may be necessitated either as the result of the dishonor of a draft which the bank holds or because of a straight consignment of merchandise to the bank. For the work of clearing the goods, storing, insuring, forwarding, and selling them, the bank engages the services of certain approved custom house brokers. In rendering this service it does not, however, take any responsibility for the safety or speedy delivery of the merchandise. Its duty is merely to transmit instructions as it receives them, using, of course, as much care as though its own interests were involved.

### **Shipments under Dishonored Drafts**

When foreign drafts accompanied by ocean bills of lading sent to the bank for collection are dishonored, the merchandise department takes charge of the shipment. The routine of customs procedure for the importer prescribe that merchandise must be "entered" at the custom house within 48 hours after the arrival of the vessel. Entry is effected by the bank's broker and consists in filing clearance papers with the customs officials on a form prescribed by the treasury department. In order to do this the broker is required to present the invoice—consular, if one has been received—and the bill of lading. If these documents are not in the possession of the bank it may give a guarantee for them under conditions to be related presently. When the broker has cleared the goods he delivers the warehouse receipt to the bank which then insures the goods against all risks under its floating policy.

### **Adjusting with the Drawee**

This procedure is followed pending final acceptance or payment of the draft by the consignee. If necessary, and if

the drawer so instructs, the case may be put in the hands of an attorney and the shipper informed of the results of the litigation. However, many drafts fail of collection for reasons of a temporary nature and it is wise to take account of these before instituting proceedings. The drawee may contend, for example, that he cannot pay the draft until a certificate of health has been issued by the Department of Agriculture to cover the consignment, or it may be that the drawee wishes to take advantage of his right to make an examination of the merchandise before deciding on payment. In such a case the bank may if it sees fit accommodate the drawee by granting him the time needed, advising the shipper of the fact in a form letter. This letter includes a clause to the effect that the bank as a result of its having authorized the entry of the goods, will not be responsible for any loss which may be sustained by the cargo while it remains undelivered to the consignee.

Sufficient time having elapsed for an inspection of the merchandise, the draft is again presented to the drawee. In case payment is made it becomes necessary merely to give the drawee a delivery order on the broker. The order specifies that the goods are to be delivered by the broker only on payment of all accrued charges, including brokerage. This closes the transaction between the bank and the drawee. The proceeds of the collection are then credited to the customer's account under advice, after the bank's commission has been deducted. This is a variable sum, depending upon the nature and amount of work undertaken on behalf of the client.

### **Merchandise under Straight Consignments**

It happens occasionally, as in the case of a rising market, that a foreign client consigns a shipment of merchandise to the bank to be held until he can dispose of it to the best advantage. In such a case the shipper makes out the docu-

ments in the name of the bank, these are transmitted to the broker for purposes of entry, and storage and insurance are effected in the usual way. Then the shipper may proceed to negotiate the cargo in whole or in part. If the client so instructs, the bank will assist him in this sale by keeping him advised as to the state of the market and by having his orders executed promptly through the broker.

As a general rule the importer is required to pay for the goods by certified check when they are delivered to him. The shipment may, however, be transferred under trust receipt. Under this arrangement the importer is required to sell the merchandise for the bank's account. There may even be a stipulation to the effect that he assign to the bank the accounts of the purchasers to the extent of the amount receivable from the importer, notice of such assignment being given to the purchasers at the time of sale.

### Guarantees and Surety Bonds

As indicated above, it becomes expedient at times to have merchandise cleared or released from a bonded warehouse, even though the relative documents have not been received by the bank, owing to delay in transit, attachment, or actual loss. Unless the merchandise is claimed immediately after its arrival it will go into "general order." Moreover, if the goods are perishable or seasonal there is double need for action in order to prevent spoliation or loss of market. The custom officials do not as a rule make delivery except against the proper documents or against a court order. However, if they feel assured that the documents have been lost or delayed and that no fraud is contemplated, they may deliver the merchandise against a guarantee of indemnity.

It is illegal for a national bank to become surety for a party unless it has a direct interest in and derives a profit from the transaction. In the case of a consignment under a draft

the goods revert to the bank as the direct representative of the drawer, should payment or acceptance be refused Under a straight consignment the bank's name appears on the bill of lading as the consignee, making it therefore the nominal owner of the goods In certain cases, too, when goods are consigned not to the bank but to one of its customers it may request the collector of the port to allow its broker to make entry of the goods and to give bond in lieu of the missing documents. Whether the bank elects to make such a guarantee will, of course, depend upon the circumstances of the case and particularly upon the credit of the client.

### **Bail Bonds**

Occasionally the bank is requested to have surety companies write so-called bail bonds for account of its clients These originate in the following manner: The law provides that ships which have been libeled for damage arising out of collision, fire, or for some other peril of the sea, be released for the benefit of the owners as soon as possible In lieu of the ship or cargo, some other good security has to be provided This is usually supplied by the use of a bail bond written by a surety company on behalf of the ship-owner Under such a bond the surety company agrees to pay any amount which may be adjudged to the plaintiff by the court.

### **Special Payments**

Foreign clients may have occasion to make payments in the United States under special conditions which require a trustworthy local agent to determine when and to what degree the conditions have been fulfilled These payments commonly arise out of the purchase by foreign shipping companies of vessels built in this country Payments may be made either on ships under construction or for vessels already completed

Payments made under contracts for the construction of

vessels are usually by instalments when prescribed stages of completion have been reached. Usually the construction cost is divided into ten instalments to be paid as follows: one each when the contract is signed, when the keel is laid, upon payment of material, when framed, when ceiled, when plated or planked, when the deck has been laid, at launching, when rigged, and when delivery is made. Either a member of the department visits the shipway, or the local agent of Lloyd's (Lloyd's Registry of Shipping) is instructed to ascertain the progress of the vessel under construction. It is desirable to send Lloyd's agent for the reason that later he will be called upon to make out the certificate of classification and for this purpose he ought to be familiar with the ship from the time the keel is laid.

Payments for the purchase of vessels already constructed are made by the bank only when the proper documents evidencing ownership, registry, etc., are delivered in accordance with the purchaser's instructions.

### **Marine Loss Claims**

Another important service consists in collecting claims under marine insurance policies. In this connection settlement of claims is made directly with the underwriters themselves. In collecting these claims the necessary documents are presented according to the needs of the case. These may consist of a full set of bills of lading, the original invoice covering the shipment, or a copy of it, the insurance certificates, the marine protest—consisting of a statement sworn to by the captain of the vessel indicating whether his ship met with any accident which would be likely to damage the goods—the deposit receipt showing that the insured has made the proper contribution to the fund out of which damage arising from general average claims is to be settled, and a certificate of damage executed by a competent surveyor or appraiser. After

its collection has been effected the proceeds are accounted for to the client in the usual way for collection

### Sundry Collections

In addition to handling claims under marine insurance, collections of a varied nature are made for the foreign client, such for example, as arise under life insurance policies, pensions, deeds, indentures, and mortgages. Customers may also route pass books and deposit receipts through the bank. These claims are either indorsed over to the bank or are accompanied by the necessary powers of attorney. In the collection of these claims the customer receives the benefit of the bank's legal department and of its counsels at law.

### INDUSTRIAL SERVICE

One of the very important services of a modern bank is rendered by what is sometimes called the "industrial service department." This department is composed of a staff of industrial engineers who travel about the country making surveys of the organization and plants of those industrial concerns which are either customers or prospective clients of the bank. The results of these surveys are embodied in comprehensive reports submitted both to the bank and to the client. Such inspections serve two main functions: (1) they supply the bank with valuable credit information, and (2) they furnish the customer with definite suggestions for the improvement of his business.

The conditions which go to make up the credit standing of a large manufacturing concern are such that they cannot be set forth completely in the form of a balance sheet and profit and loss statement. Many considerations not shown in figures are of tremendous importance. Among these may be mentioned location of the factory with respect to raw



materials, labor supply, and markets, labor conditions in the plant, management, system of cost-finding, pricing, and many other rather intangible factors. The industrial service engineers obtain and interpret these facts for the credit department of the bank.

The industrial engineers, however, serve a far more important function than that of acting as mere expert investigators for the credit department of the bank. Their calls upon customers are made primarily with the idea of furnishing service. Hence quite as frequently as not they make surveys of establishments of customers which do not need bank credit or even of concerns which are not customers of the bank. By experience reaped from long contact with manufacturing concerns in all lines of activities such industrial engineers are enabled to analyze a business, to bring out its strong points, and to make suggestions for the improvement of its weak ones. In this way such a department can accumulate a wealth of figures and statistics covering such standard figures for each industry as cost of production, proportion of each item making up cost, profits, etc., which may be placed at the disposal of the clients. Recommendations as to methods of accounting, financing, purchasing, selling, paying wages, etc., can be embodied in comprehensive reports furnished to the customer.

In addition to furnishing an individual customer with specific advice on his own problems, such an industrial service department performs a somewhat more general service for the clients of the bank as a whole. This service takes the form of published studies and reports on the common problems of manufacturers which are distributed by the publicity department. The industrial engineers can also represent the bank at conventions of manufacturers and others interested in scientific methods of production.

In summary, a department of this sort is a safeguard

against injudicious loans, a means of promoting cordial relations between the bank and its family of industrial customers, and a protection to industry as a whole, since it advocates a scientific basis of doing business on the basis of cost rather than of competition.

## CHAPTER XXVIII

### ORGANIZATION AND ADMINISTRATION

#### Officers and Board of Directors

The corporate affairs of a national bank are especially interesting because national banks are among the few corporations organized under federal law in this country. This control is vested in the owners of the corporation—the shareholders. The shareholders elect a board of directors which in turn elects and appoints certain officers to execute its will and policy. The offices, number of incumbents, and the duties of each vary with the size of the bank, the character of its business, and the types of men who hold offices. Officers commonly found in the largest banks are

- 1 The president, who is usually chairman of the board of directors
2. The executive managers, one of whom may be designated as general executive manager.
- 3 Vice-presidents
- 4 Trust officers
- 5 The comptroller.
- 6 The cashier.
- 7 Assistant vice-presidents.
- 8 Assistant cashiers
- 9 Assistant trust officers
- 10 Assistant comptrollers.

#### Shareholders

The minimum capitalization of a national bank is based upon the population of the city or town in which the bank is

domiciled <sup>1</sup> There is no limit to the number of shares which may be owned by each holder except as results indirectly from limitations as to the number of incorporators. Stockholders of national banks are financially liable for all contracts, debts, and engagements of the bank to an amount equal to twice the par value of stock owned. Otherwise they have much the same relation to the bank as the stockholders of any other kind of corporation organized under the laws of a state have to their corporation.

The procedure which shareholders follow in controlling the affairs of the bank is set forth in the bank's charter which must be approved by the Comptroller of the Currency before the bank begins business.

When there is any action to be taken which may require the consent of the shareholders, their assent unless unanimous must be given at a duly convened meeting. It does not suffice to secure in writing the assent of shareholders owning enough stock to pass the action, no majority can bind a minority, however large the majority or small the minority unless the action is taken in a duly called meeting. The charter provides for both regular and special meetings. Each shareholder has a right to be present in person or by proxy and to express his assent or dissent. However, no officer, clerk, teller, or bookkeeper of the bank may act as proxy and the Comptroller of the Currency has ruled that directors may not act in this capacity within the intent of this law. Shareholders who have due and unpaid subscriptions for stock are disqualified from voting. Each shareholder is entitled to one vote on each share of stock held by him. A majority of the shareholders present in person or by proxy constitutes quorum.

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<sup>1</sup>The present requirements are as follows

For cities of	not over	3,000,	\$ 25,000
" " " " "	6,000,	50,000	
" " " " "	50,000,	100,000	
" " " " "	60,000,	200,000	

### Annual Meeting

Among the most important powers of the shareholders is the election of the board of directors which manages the affairs of the bank. The board is elected annually at what is commonly called the "annual meeting." The annual meeting of national banks may be held on any day in January but the Comptroller of the Currency favors the second Tuesday. At this meeting no other business but the election of directors may be transacted without due notice having been given that other business is to be transacted. If the bank fails to effect an election at the time appointed, an election may be held on any subsequent day after 30 days' notice thereof has been given in a local newspaper. The date of election is fixed in the charter by the directors or by two-thirds of the shareholders. The directors therefore cannot continue to hold office by failing to hold an election, for the shareholders can convene and fix the date thereof.

Ultimate control of the management of the bank is thus vested in the stockholders. Unless two-thirds of them are dissatisfied with the incumbent board the directors may retain office indefinitely by mere default of the shareholders to force an election.

### Qualifications of Directors

National banks are required to have a board of not less than five members, but no maximum number is fixed. Banks in larger cities have more than five, the purpose being not only to distribute the burden of the administrative work, but also to secure a more representative board and thus create a larger good-will in the community. The directors are elected at the annual meeting for a term of one year and until their successors are elected and have qualified.

Every director of a national bank must during his whole term of office be a citizen of the United States, and at least

three-fourths of the directors must have resided in the state, territory, or district in which the bank is located for at least one year immediately preceding their election and must be residents therein during their continuance in office. These residential and citizenship qualifications give local control to the bank and assure a better adaptation of its policy and conduct to the needs of the community as well as safeguarding the control of the bank against adverse interests. Every director must own in his own right at least ten shares of stock of the bank, unless the capital of the bank does not exceed \$25,000 in which case he must own five shares. Any director who ceases to own the required number of shares or who becomes in any other manner disqualified, vacates his directorship thereby. No person who holds stock in a merely representative capacity, as trustee, executor, administrator, or guardian, can be a director. These property qualifications aim at giving the directors a personal interest in the successful conduct of the bank.

The Clayton Act provides that no person shall at the same time be a director or other officer or employee of more than one member bank of the federal reserve system when either of these banks has deposits, capital, surplus, and undivided profits aggregating more than \$5,000,000, and no private banker or person who is a director in any state bank having deposits, capital, surplus, and undivided profits aggregating more than \$5,000,000 is eligible to be a director in any member bank of the system. Furthermore no member bank in a city of more than 200,000 inhabitants may have as director or other officer or employee any private banker or any director of any other bank, banking association, or trust company located in the same place, with the following exceptions (1) this provision does not apply to mutual savings banks without capital stock, (2) a director or other officer or employee of such bank, banking association, or trust company may be a

director or other officer or employee of not more than one other bank or trust company organized under the laws of the United States or any state where the entire capital stock of one bank is owned by stockholders in the other, and (3) a director of Class A of the federal reserve bank may be an officer or director or both in one member bank

The Clayton Act was amended by the Kern Amendment in 1916 which permits any officer, director, or employee of any member bank or Class A director of a federal reserve bank who first procures the consent of the Federal Reserve Board to be an officer, director, or employee of not more than two other banks, banking associations, or trust companies, whether organized under the laws of the United States or any state, if such other bank, banking association, or trust company is not in substantial competition with such member bank. The board is authorized, at its discretion, to grant, withhold, or revoke such consent, and the authority requires it to define what constitutes substantial competition. Another amendment permits any director or other officer, agent, or employee of any member bank with the approval of the Federal Reserve Board, to be a director or other officer, agent, or employee of any bank or corporation chartered under federal or state law and principally engaged in international or foreign banking or banking in any dependency or insular possession of the United States in the capital stock of which the member bank has invested as allowed by law. The substance of this amendment was reiterated in the Edge Act to permit officers, directors, and employees of member banks to become affiliated on the approval of the Federal Reserve Board with a corporation authorized under the act provided the member bank is itself a stockholder in such corporation. The law was further amended in 1917 to the effect that a state bank becoming a member may continue to exercise its full charter and statutory rights as a state bank or trust company which amendment

exempts it from certain of the provisions of the above laws.

The directors are put under oath diligently and honestly to administer the affairs of the bank and to be qualified. These oaths are sent to the Comptroller of the Currency and filed.

A director is not an agent of the bank, he cannot act separately and independently of his fellow-members. Only when the board is duly convened and acting as a unit does it represent the bank. At such time it may appoint one of its number to act as agent of the bank. A majority of the board usually constitutes a quorum but this is determined by the charter provisions.

### Remuneration of Directors

Directors normally serve without salary. Since as a rule they are men of wide business interests, the time and attention required of a bank director entails a considerable sacrifice. In some large banks directors are given fees for each meeting they attend, but these fees do not compensate them for the sacrifice of time. The banking law prohibits any officer, director, or employee of a member bank from being the beneficiary of or receiving directly or indirectly any fee, commission, gift, or other consideration for or in connection with any transaction or business of the bank, other than the usual reasonable salary or director's fee paid to him for services to the bank.

In choosing directors various factors are considered. The largest stockholders may be elected, the other shareholders feeling that their large holdings will incline them to take a keen interest in the success of the bank, or men of large influence in the community or of large capital and business connection may be elected for the business which they will bring to the bank. It is highly important that they be men of good financial record and possessed of conservative business sense and sound judgment.



## **Powers of Board of Directors**

The board exercises the general control and government of all the affairs and transactions of the bank. With a few restrictions it can do anything the corporation can do under its charter and the law. The functions which the board must perform are largely determined by the uniform usage among banks. The members must, i e., handle the active management of the bank, they are assumed to know all that is done and the system and rules for doing it, they may appoint agents and endow them with powers sufficient for executing the resolutions of the board and for carrying out the ordinary transactions of daily business without specific authority in each instance. Such delegation of power, however, does not divest the directors of their responsibility and duty and they may be held for losses arising through the action of officers when in the selection and supervision of these officers the board is proved not to have acted in good faith or with ordinary diligence.

The courts distinguish between executory functions and management functions. The former are the media through which management and control are effected and consist of such acts as drawing checks, receiving deposits, paying drafts, etc., and may be done by the duly appointed officers without an authorizing vote by the directors.

## **Liability of Directors**

The courts regard the directors as trustees for the stockholders and for depositors and noteholders. They insist not only that the directors be free from blame but that they be prohibited from doing things where self-interest may bias them against the bank. A director is not permitted to secure by means of his trust any advantage not common to the other stockholders. In all such matters he must both refrain from voting and exercising his influence. If he applies for a loan

he must not vote on the approval of his application and must behave as any other applicant

The directors cannot do certain things. They can use the funds and property of the bank only for proper banking functions and for the bank's advantage in the best way that their knowledge and abilities can devise. They cannot vote to contribute to charities or make gifts. They cannot needlessly and gratuitously assume actual or contingent liabilities for others.

Directors are liable for losses to stockholders or creditors, or both, incurred because the directors fail to manage the bank according to the charter and in good faith. They are not liable for losses arising through frauds by officers provided they have not been grossly negligent in selecting and watching such officers. What constitutes reasonable care required of directors depends upon the matter in hand and can only be determined in the light of all circumstances. Ill health or non-residence does not excuse a director from constructive knowledge of the affairs of the bank.

In keeping with these responsibilities the directors of a bank exercise more personal control over their corporation than is usually the case in other types of corporations. In the bank upon the practices of which this book is written, for example, the directors meet each week for the purpose of considering the financial position of the bank and determining its policies. The making of loans and the granting of credit are matters which are closely supervised by the directors. For the purpose of facilitating its work the board operates through committees, such as the loan committee, executive committee, etc.

### **The President**

The president of a national bank is elected by the board of directors and by law he must be chosen from among their own number. Usually his duty is to preside over the meetings

of the board. In addition he may be given active management of the bank's affairs. The larger banks often divide this office into two parts. A chairman of the board is elected to preside over meetings of the board of directors, while the president serves as manager of the bank.

So far as managerial powers go, the position of the president is one of dignity and of an indefinite responsibility rather than of accurately defined duties. His *ex officio* powers are scarcely greater than those of any other director. As head of the board he may bring suit in the name of the bank, and in suits against the bank legal processes may be served upon him. The responsibility for the litigation of the bank, both as plaintiff and defendant, is inherent in his office and for this purpose he may retain and employ counsel. This is his sole inherent power beyond that of any other director. But he is commonly the active executive officer of the bank and his authority is very much extended by express delegation by the board or by their tacit sanction of his known acts.

The foregoing discussion applies in general to all banks. Following the office of president, the scheme of organization depends entirely upon the needs of a particular bank as no generalizations can be made. A description of the organization of the bank on which the practices described in this book are based will therefore be given.

### **The Executive Managers**

To assist the president in the active administration of the bank, a group of executive managers, one of whom is designated general executive manager, has been created. These officers are chosen from among the vice-presidents and they include men of wide experience and broad knowledge in banking. In other words they are technical or practical bankers to whom are delegated the supervision of certain phases of the actual operation of the bank. The parcellation of duties

among the executive managers varies with the personnel of the group. The general executive manager is in general the active manager of the bank. Others of the executive managers specialize in fields of management for which they have shown special aptitude.

### **The Vice-Presidents and the Territories**

The unit of administration in the bank is the territory. The bank has divided the domestic territory on the basis of federal reserve districts and the foreign territory on the basis of contiguous countries. To maintain a close personal touch with its customers, all the business of a particular territory is administered by a vice-president assisted by the necessary number of assistant vice-presidents and assistant cashiers. The vice-president is responsible both for maintaining and extending the business of the bank in his territory. In the domestic field he controls the resident representatives of the bank in the territories where they work for the purpose of extending its business, obtaining credit information, etc. In the foreign field the vice-president in charge controls the branches and agencies of the bank.

The activity of the territorial group of officers consists of two parts. (1) passing upon loans, and (2) service and new business. Subject to review by a general meeting of the officers of the bank and by the directors in their weekly meeting, the vice-president passes upon all applications both for loans and for lines of credit arising within his territory. Certain of the assistant vice-presidents and the assistant cashiers assigned to assist the vice-president in the territory are credit men. Often they have resided in the territory and know personally many of the customers of the bank and the conditions under which they transact business. By this method of passing upon loans, the bank aims to give the customer the advantage which comes from a personal acquaintance with

him and his affairs by someone in high authority in the institution

The vice-president is also responsible for developing new business in his territory. In this development the bank seeks not only to obtain new accounts but also to intensify its relations with those who are already its customers. Service assistants consisting of officers and others attached to the territorial organization devote their time to considering the use which customers make of their accounts and to bringing other services of the bank to their attention. In other words, the service assistants seek to help each customer obtain the maximum advantage from his connection with the bank and also to see that each customer's account is a source of profit to the bank.

New business prospects come to the attention of the bank in a variety of ways. The most important agencies for seeking out desirable customers are the branches of the bank and the domestic field men. Again prospective customers often apply to the bank for service which its more or less distinctive facilities enable it to render, such as the foreign trade service, foreign exchange transactions, collections, credit information, etc. If the applicant is of the type which the bank desires as a customer, the service applied for is furnished through the territorial organization and an effort is made to extend relations with him. The publicity department is also an effective agency for bringing the services of the bank to the attention of those who may become customers. Prospects are also obtained from the reports of the credit agencies.

In order that its relations with customers may be cordial and at the same time conducive to mutual profit, the bank makes a careful investigation of each prospect before it solicits his account. This investigation aims to ascertain whether or not the prospect can profitably open a New York account. The field of the metropolitan bank and that of the local cor-

respondent are mutually exclusive and the former can solicit business without taking it away from the latter. If the prospect has not a real need for an account in a large bank and if his business is not such that both he and the bank will derive a profit from an account relation, he is not solicited. The bank considers that it avoids needless embarrassment and complications in the future by knowing the facts before it enters into negotiations with a prospect.

After this investigation is made the procedure is governed by the vice-president in charge of the applicant's territory. The ruling on a name is: (1) do not solicit, (2) deferred, or (3) approved. Names which the vice-president has classed as undesirable are dropped. Deferred names are not to be solicited at the time but they are to be watched with a view to considering them again.

Actual solicitation of the new name is made by the field men or the foreign representatives of the bank through personal calls and by the service of new business men in the territorial organization. Often some by-service of the bank is put at the disposal of the customer with a view to convincing him of the type of work which the bank is capable of doing.

**Other Vice-Presidents, Assistant Vice-Presidents, the Assistant Cashiers, Assistant Trust Officers, and Assistant Comptrollers**

While the majority of the vice-presidents, assistant vice-presidents, and assistant cashiers are assigned to the territorial administrative units, others handle certain of the operating departments of the bank according to their aptitude and adaptabilities. A vice-president assisted by assistant vice-president, for example, does the trading in foreign exchange. Another vice-president assisted by the statistician has charge of the publicity work, another of the trust department, another of a very important foreign branch, still others travel and

devote their time and attention to the study of economic conditions. An assistant vice-president has charge of the credit department, another of the letter of credit department, and another of the industrial service work, while assistant cashiers are assigned to manage other important divisions and departments in the bank. Junior officers, known as assistant trust officers, assist the vice-president in charge of the trust department, while others, known as assistant comptrollers, assist the comptroller of the bank.

### The Comptroller and Cashier

In general the executive work of the bank (if distinction may be made between executive and administrative work) is divided between the comptroller and the cashier. The work of the comptroller is that of supervising accounting and auditing and he has control of the expenses of the bank. An equally important part of his work consists in supervising systems in use in the bank and its branches. The cashier is the chief executive officer through whom the financial operations of the bank are conducted. As such he has charge of all the operating departments of the bank. He also exercises supervision over the personnel and its organization and over the building force.

To assist the cashier of the bank in matters of organization, an organization department is maintained. The chief function of this department is to study the departmental work with a view to making improvements. It also makes studies of the personnel with a view to discovering those who are worthy of promotion to positions of greater responsibility.

### Departments and Divisions

The unit of operation in the bank is the department, one of which performs each major operation. Each department is in charge of a department head with a sufficient number of assistant department heads. Related departments are grouped

together into divisions, each of which is supervised by a division head. Through the organization department the division heads are responsible to the cashier of the bank. Matters of operating procedure are referred to them by department heads. In addition they have charge of the personnel in their respective provinces. At regular intervals a meeting of the division heads is held by the organization department for the purpose of considering improvements in the operating routine, organization, etc.

### **Branch Banks**

By the National Bank Act a national bank is prohibited from operating domestic branches except where it previously existed as a state bank and had branches under the laws of its state. The Federal Reserve Act permits member banks to have foreign branches, however. In accordance with this law the bank concerning which this is written has organized branches in many of the principal cities abroad.

Each branch bank is under the control of the vice-president in whose territory it is located. Local management of the branch is vested in a manager who is assisted by the necessary number of submanagers, an accountant, and subaccountants. The small branches in a locality are in some cases grouped together under the local control of a large branch.





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